TRANSCRIPT OF RECORD

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1940

No. 393

THE UNITED STATES, PETITIONER

vs.

ARTHUR PELZER

ON WRIT OF CERTIORARI TO THE COURT OF CLAIMS

PETITION FOR CERTIORARI FILED SEPTEMBER 3, 1940
CERTIORARI GRANTED OCTOBER 21, 1940

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ON PETITION FOR A WRIT OF CERTIORARI TO THE COURT OF CLAIMS

INDEX

259228—40——1

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1 In United States Court of Claims

No. 43923

ARTHUR PELZER, PLAINTIFF

vs.

THE UNITED STATES OF AMERICA, DEFENDANT

I. Petition

Filed April 29, 1938

Comes now the plaintiff, Arthur Pelzer, by his attorney, Robert A. Littleton, and respectfully shows to the Court:

1. That plaintiff is a citizen and resident of the United States and resides at Montgomery, in the State of Alabama.

2. On the 14th day of July 1932, the plaintiff created an irrevocable trust for the benefit of his eight grandchildren then living, viz: Weldon W. Doe, Jr., Alice Pelzer Webber, Camilla Webber, Amelia K. Webber, Arthur Pelzer Webber, Elizabeth Joseph, Alice Joseph, and W. F. Joseph, Jr. In creating said trust the plaintiff
2 deposited with the trustee named property of the value of $49,998.83.

3. In paragraph 2 of said trust instrument it is provided that for a period of ten years from and after the date of July 14, 1932, the net income from the corpus of the trust be accumulated and invested and reinvested from time to time by the trustee; and that after the expiration of ten years the trustee is required to distribute the net income from the trust to each of the trustor's grandchildren named above who may then be living and be twenty-one years of age or over in proportion to the number of grandchildren then living, whether born before or after the date of July 14, 1932.

4. It is provided in said trust instrument that in the event of the death of any of the beneficiaries specifically named in said instrument, without leaving issue, then, and in that event, the interest of the deceased beneficiary in the trust property shall belong to his surviving brothers or sisters, if any, and if none, then to the other grandchildren of the trustor per stirpes, subject to the terms of the trust.

5. The period of the trust is for twenty-one years after the death of the last survivor of all of the trustor's grandchildren who are living at the date of July 14, 1932, whose names are set forth in the trust instrument, at which time the trust shall cease and determine, and the corpus of the trust, with any accumulation, shall then be
3 distributed to the grandchildren of the trustor, born after the date of July 14, 1932, and who may at that time be living (each such living grandchild to receive a grandchild's equal share), and the issue of all deceased grandchildren to receive the deceased parent's share of the trust property per stirpes.

6. Section 504 (b) of the Revenue Act of 1932 provides as follows:
"In the case of gifts (other than of future interests in property) made to any person by the donor during the calendar year, the first $5,000 of such gifts to such person shall not, for the purposes of subsection (a), be included in the total amount of gifts made during such year."

7. In making a return of the gifts evidenced by the trust instrument of July 14, 1932, to the eight grandchildren of the donor therein named, the plaintiff omitted to claim an exclusion of $5,000 for each of the named beneficiaries; but did claim a specific exemption of $50,000 which left no net value of said gifts subject to tax.

8. Plaintiff avers that in reporting the 1932 gifts, as aforesaid, for tax purposes, he is entitled to eight $5,000 exclusions in the aggregate amount of $40,000, and that inasmuch as only $9,998.83 of the specific exemption of $50,000 allowable is absorbed by the 1932 gifts the balance of such specific exemption of $40,001.17 is allowable in a subsequent year or years.

9. Plaintiff avers that during the calendar year 1933 he made
4 further gifts to the beneficiaries named in said trust instrument in the aggregate amount of $29,800 together with three additional gifts of $6,000 each to the following named persons, viz: Francis P. Doe, Elizabeth K. Webber, and Alice E. Joseph. That the gifts of 1933 amounted to the aggregate of $47,800.00, of which only $3,000 is the net amount subject to tax, which is absorbed by the specific exemption of $40,001.17 carried over from the year 1932. Plaintiff is not liable for a gift tax for the year 1933.

10. Plaintiff avers that during the year 1934 he made gifts in the aggregate amount of $38,803.00 to the persons named in the trust instrument of July 14, 1932; gifts in the aggregate amount of $153,060.00, in trust for the following named beneficiaries, viz: Eva L. Pelzer, Francis P. Doe, Elizabeth K. Webber, and Alice E. Joseph, and gifts in the amount of $6,000 each to the following named persons, viz: Francis P. Doe, Elizabeth K. Webber, and Alice Joseph. That no part of the 1934 gifts, in the aggregate amount of $38,803.00, is subject to tax because of the eight $5,000 exclusions allowable. That from the 1934 gifts in the aggregate amount of $153,060.00, four $5,000 exclusions are allowable, which leaves $133,060.00 of such gifts subject to tax; and from the gifts in the aggregate amount of $18,000, three $5,000 exclusions are allowable, which leaves $3,000 of such gifts subject to tax. For the year 1934 there was $37,001.17 of the specific exemption of $50,000 unused by gifts in prior years, and after
5 the same is allowed from the 1934 gifts in the aggregate amount of $138,060.00 after exclusions, the net amount of such gifts subject to tax is $101,058.83.

11. Plaintiff avers that during the year 1935 he made gifts in the aggregate amount of $39,531.25 to the persons named in the trust instrument of July 14, 1932, under which he is entitled to eight exclu-

sions in the amount of $5,000 each, which leaves no part of said gifts subject to tax.

12. Plaintiff avers that the total net gifts during the years 1932, 1933, 1934, and 1935 upon which a gift tax is due is the aggregate amount of $101,058.83; whereas, the Commissioner of Internal Revenue has erroneously computed the net amount of said gifts subject to tax to be $242,193.08, and assessed and collected a tax thereon in the aggregate amount of $16,681.70. The correct amount of the tax for which plaintiff is liable on the net value of said gifts for all years is the sum of $3,693.82; but through error there has been collected from plaintiff by the Treasury Department of defendant the aggregate amount of $16,681.70 together with interest in the amount of $465.45.

13. On November 25, 1935, plaintiff paid a tax of $533.96 and accrued interest of $53.54 computed by the Bureau of Internal Revenue on net value of gifts for the year 1933. On the return of the net value of gifts for the year 1934, plaintiff computed and paid in March 1935, a tax of $4,538.82 and thereafter the Bureau of Internal Rev-
6 enue determined an additional tax of $6,865.17 on the net value of the gifts for 1934, which plaintiff paid on March 14, 1936, together with accrued interest in the amount of $411.91. On the return of the net value of the gifts for the year 1935, the plaintiff paid a total of $4,743.75 on March 15, 1936.

14. On July 27, 1937, the plaintiff filed claims for the refund of $587.50 tax and interest paid for the year 1933; of $7,277.08 tax and interest paid for the year 1934; and of $4,743.74 tax and interest paid for the year 1935.

15. On or about January 17, 1938, the Commissioner of Internal Revenue acted upon said claims and allowed the claim for the year 1933 in the amount of $270.07, and rejected same in the amount of $317.43; allowed the claim for the year 1934 in the amount of $1,011.25, and rejected it in the amount of $10,804.65, and allowed the claim for the year 1935 in the amount of $600 and rejected it in the amount of $4,143.75.

16. Plaintiff avers that he is not liable for a gift tax for the years 1932, 1933, and 1935, and the amount of the gift tax due and payable for the year 1934 is the amount of $3,693.82. That there has been erroneously and illegally collected from the plaintiff for the years 1933, 1934, and 1935 a gift tax and interest in the aggregate amount of $13,453.33, for which he prays judgment of this Court, together with interest from the dates of payment as aforesaid, less refunds heretofore made.

7 17. Plaintiff avers that he has at all times borne true allegiance to the United States; that he is the true and lawful owner of the claim sued upon, that the same has not been assigned, that there are no offsets or counterclaims thereto, that said claim is due and owing to the plaintiff; and that no claim therefor has been made except as stated above.

Wherefore, plaintiff sues the defendant for the amount of $12,453.30, less refunds heretofore made, together with interest thereon from the dates of payment above stated, for which amount judgment is prayed.

ROBERT A. LITTLETON,
Attorney for Plaintiff,
1021 Tower Building, Washington, D. C.

[*Duly sworn to by Arthur Pelzer; jurat omitted in printing.*]

9 *II. General traverse*

Filed June 7, 1938

And now comes the Attorney General, on behalf of the United States, and answering the petition of the claimant herein, denies each and every allegation therein contained; and asks judgment that the petition be dismissed.

JAMES W. MORRIS,
Assistant Attorney General.

III. Argument and submission of case

On January 10, 1940, this case was argued and submitted on merits by Mr. Robert A. Littleton for plaintiff, and by Mrs. Elizabeth B. Davis for defendant. Littleton, J., did not participate.

IV. Special findings of fact, conclusions of law, and opinion of the court by Williams, J.

Filed March 4, 1940

10 Mr. Robert A. Littleton for the plaintiff.

Mrs. Elizabeth B. Davis, with whom was Mr. Assistant Attorney General Samuel O. Clark, Jr., for the defendant. Mr. Robert N. Anderson was on the brief.

The court, upon the stipulation of facts and the evidence, makes the following

SPECIAL FINDINGS OF FACT

1. The plaintiff, Arthur Pelzer, is a citizen of the United States and a resident of Montgomery, Alabama.

2. On July 14, 1932, the plaintiff executed a trust instrument, which is hereinafter referred to as the "children's trust." This instrument, after reciting that the trustor (the plaintiff) was transferring certain personal property to the trustee in trust for the use and benefit of the trustor's living grandchildren (eight in number, being specifically named) and other grandchild and/or grandchildren of the trustor as might hereafter be born during the life of the trust, provided: first, the trustee was to manage the property, to sell and to invest and

reinvest the proceeds from sales with the provision that he should consult with the trustor about investments and changes in and disposition of the trust property, it being distinctly agreed, however, that by this it is not intended, nor shall it be construed to be intended, that the Trustor shall have any right to change any of the terms of
11 this instrument, or distribution of the trust estate, nor any right to revoke or change any provisions hereof, nor be entitled to receive any economic, financial, or other benefit from the trust estate." It is further provided that the trustee shall collect the income and pay expenses and distribute the net income in the manner thereinafter stated.

Paragraphs 2, 3, and 4 (Exhibit A) of the trust instrument are as follows:

"2. For a period of ten years from date hereof the net income from this trust estate shall by the Trustee be accumulated and invested and reinvested from time to time. At the expiration of said ten years the Trustee shall thereafter pay in semiannual, quarterly, or monthly installments (whichever is more practicable) an equal grandchild's distributive share of the net income from this estate to each of the Trustor's now living grandchildren whose names are set out above, who may be then living and be twenty-one years of age or over, said payments to continue to each during his and/or her respective life; and as and when each of Trustor's remaining grandchildren who are now living, and whose names are hereinabove set out, respectively reaches the age of twenty-one years, the Trustee shall thereafter pay in said semiannual, quarterly, or monthly installments to him and/or her for and during his and/or her respective life an equal grandchild's distributive share of the net income from the trust estate; but, in the meantime, and during the respective minority of the remaining of the hereinabove specifically named now living grandchildren, all net income not required to be paid out under the terms hereof to adult grandchildren and to or for grandchildren hereafter born, shall be invested and reinvested according to the terms of this instrument to the end that the net trust income may be accumulated during the period authorized by law.

"Should the Trustor have other grandchildren born hereafter during the life of this trust, then each and all of said hereafter born grandchildren shall be entitled to participate in the trust estate equally with the other grandchildren hereinabove named, and to receive an equal grandchild's distributive share as herein provided, except as to distributions of net income that may have been made prior to the birth of such hereafter born grandchild or grandchildren; provided, however, and except further that for ten years from the date hereof, the net income from this estate shall be accumulated and in-
12 vested and reinvested as hereinabove provided, and subject further to the terms of this trust. At the expiration of ten years from date, then as to any and all of Trustor's grandchildren who may be hereafter born and then living, the Trustee shall thereafter

during the life of this trust pay in said periodical installments to or for each of said now unborn, but hereafter born grandchildren if then living, an equal grandchild's distributive share of the net income from this trust estate. Such payment of net income shall be made direct to each after born grandchild when and after he or she reaches twenty-one years of age, and during the minority of such after born grandchild may be paid out or expended directly by the Trustee for the support, maintenance, comfort, and education of such grandchild, or be paid by the Trustee to the mother thereof for said purposes.

"3. Should any of the grandchildren of Trustor die during the life of this trust without leaving issue, then said deceased grandchild's distributive share of the net income hereunder shall belong to his and/or surviving brother and/or sister, if any, and if none, then to the other grandchildren per stirpes, subject to the terms of this trust; but should any of the grandchildren of Trustor die leaving issue, then said issue shall be entitled to receive the deceased grandchild's share of the income per stirpes, subject to the terms of this trust. During the life of this trust, all net income payable by the Trustee to or for the issue of a deceased grandchild shall be paid by the Trustee to or for him at the time and in the manner hereinabove at the end of the preceding paragraph provided in the case of a grandchild.

"4. This trust shall continue, and the income therefrom be distributed as hereinabove provided, until twenty-one years after the death of the last survivor of all of Trustor's grandchildren who are now living, and whose names are set forth hereinabove, at which time it shall cease and determine, and the corpus, with any accumulation, shall then be distributed free from this trust among such, if any, of Trustor's grandchildren born hereafter who may at that time be living (each such living grandchild to receive a grandchild's equal share), and the issue of all deceased grandchildren, the issue of a diseased grandchild, to receive the deceased parent's share per stirpes."

The remaining provisions of the trust instrument deal with the substitution of a trustee if the trustee named resigned or died, the giving of bond by the trustee, etc., which provisions are not material to a decision of this case.

13 3. On March 15, 1933, the plaintiff filed a gift tax return for the year 1932, showing total gifts for that year in the amount of $50,000 on account of transfers made by the plaintiff to the trustee of the children's trust during that year and claiming a specific exemption of $50,000, resulting in no net gifts and no gift tax for the year 1932. In an audit of this return the Commissioner of Internal Revenue determined the total gifts for 1932 to be $49,998.83 and allowed a specific exemption in a like amount, resulting in no net gifts and no gift tax for that year. Plaintiff was notified of this audit on January 18, 1935.

4. On March 15, 1934, plaintiff filed a gift tax return for the year 1933, showing total gifts in the amount of $18,000 representing three gifts of $6,000 each to plaintiff's daughters, Frances P. Doe, Elizabeth

K. Webber, and Alice E. Joseph, from which was deducted three exclusions of $5,000 each, resulting in gross gifts for that year of $3,000 from which was deducted a specific exemption of $3,000, resulting in no net gifts and no tax due for that year.

When the Commissioner of Internal Revenue audited plaintiff's gift tax return for the year 1933 he determined that the total gifts made by plaintiff for the year 1933 amounted in the aggregate to $47,800, and that in addition to the three gifts of $6,000 each to Frances P. Doe, Elizabeth K. Webber, and Alice E. Joseph, reported in said return, the amount of $29,800 transferred to the trustee of the children's trust should be included in the 1933 gifts. The Commissioner, in said audit for 1933, allowed three exclusions of $5,000 each; and computed gross gifts by plaintiff for 1933 in the amount of $32,800 from which he allowed a specific exemption of $1.17, being the unused portion of the specific exemption of $50,000 carried over from the year 1932.

As a result of the foregoing changes made in the plaintiff's gift tax return for the year 1933, the Commissioner determined a gift tax liability against plaintiff for the year 1933 in the amount of $533.96, plus interest thereon in the amount of $53.54, which tax and interest was paid by plaintiff on November 27, 1935.

5. On December 28, 1934, the plaintiff executed a trust instrument, hereinafter referred to as the "adult trust." This agreement,
14 after reciting that it was an irrevocable trust indenture between the plaintiff as trustor and the trustee by which the trustor transferred certain personal property to the trustee in trust for the use and benefit of the Trustor's wife and daughters (Eva L. Pelzer, his wife, Frances P. Doe, Elizabeth K. Webber, and Alice E. Joseph, his daughters), provided: first, that the trustees should manage the property and should have the right to change or sell and to invest and reinvest the proceeds from the sale but should confer with the trustor about investments and changes in and disposition of the trust property, "it being distinctly agreed between the parties, however, that by this it is not intended, nor shall it be construed to be intended, that the Trustor shall have any right to change any of the terms of this instrument or distribution of the trust estate, nor any right to revoke or change any provision hereof, nor be entitled to receive any economic, financial, or other benefit from the trust estate."

Paragraphs 3 and 4 (Exhibit B), of the trust instrument are as follows:

"3. The net income from said trust estate shall be paid to the said beneficiaries, Eva L. Pelzer, Frances P. Doe, Elizabeth K. Webber, and Alice E. Joseph, share and share alike, in quarterly installments, adjustments to be made from time to time according to the earnings of the trusts.

"Upon the death of Trustor's wife, her share of the income shall be divided equally among all of Trustor's grandchildren; and upon the death of any of Trustor's daughters, her share of the income shall

259228—40——2

go to her children in equal shares. In the event of the death of any grandchild leaving issue, such grandchild's share hereunder shall go to such issue, and if no issue, to such grandchild's heirs at law. Any payment required hereunder to be made to a grandchild, or issue of a grandchild, who may be under twenty-one years of age may be paid by the Trustee to the parent of such grandchild, if living, for his or her benefit until arrival at age twenty-one; and if the parent of such grandchild is not living, any payment required hereunder may be disbursed by the Trustee in its discretion for the benefit of such grandchild until arrival at age twenty-one; and paid direct thereafter.

"4. Said Trust shall continue throughout the lives of the several beneficiaries hereinabove named, and upon the death of any, the share of said deceased beneficiary shall continue in trust for the chil-
15 dren or grandchildren of said beneficiary, share and share alike, as set forth herein; that is, the one-fourth share of Trustor's wife shall continue in trust for all the grandchildren of the Trustor, share and share alike, and the one-fourth share of any of the daughters of said Trustor dying shall continue for the children of said daughter, share and share alike; if any, and if none, for her heirs at law, to be finally distributed as hereinafter provided.

"Upon arrival of any of the grandchildren of Trustor at the age of twenty-two, said grandchild's grandmother being deceased, or upon her decease thereafter, this trust shall cease and determine as to that grandchild's share of the one-fourth of this trust held for the benefit of Trustor's wife; and said share shall be paid over to said grandchild free of this trust, to the end that upon the arrival of the youngest of Trustor's grandchildren at the age of twenty-two years, said Trustor's wife being deceased, this trust shall cease and determine as to said one-fourth; and similarly, upon arrival of any of the grandchildren of Trustor at the age of twenty-two years, said grandchild's mother being deceased, or upon her decease thereafter, this trust shall cease and determine as to that grandchild's share of the one-fourth of this trust held for the benefit of his or her mother (which shall be an equal share with the other issue of his or her mother); and said share shall be paid over to said grandchild free of this trust, to the end that upon the arrival of the youngest of the issue of the deceased daughter of Trustor at the age of twenty-two years, this trust shall cease and determine as to such deceased daughter's one-fourth. In the event of the death of a daughter leaving no issue, her share hereunder shall go to her heirs at law."

The remaining provisions of the trust deal with the various rights of the trustee, the giving of bond and the substitution of trustee, which provisions are not material to a decision of this case.

6. On March 15, 1935, the plaintiff filed a gift tax return for the year 1934 showing total gifts in the amount of $209,863. Of this amount, $153,060 was paid to the trustee of the "adult trust," $6,000 to each of the trustor's daughters, Frances P. Doe, Elizabeth K. Webber, and Alice E. Joseph, and $38,803 to the trustee of the "chil-

dren's trust." On this return plaintiff claims specific exclusions of 358,803 and a specific exemption of $37,001.17, resulting in total net gifts of $114,053.83 and a tax of $4,538.82.

16 On March 14, 1936, plaintiff filed an amended gift tax return for the year 1933 showing total gifts in the amount of 3209,863 (the same as shown on the original return) from which was deducted specific exclusions in the amount of $20,000, leaving net gifts for the year of $189,863, resulting in a tax due of $11,403.99. Inasmuch as a tax of $4,538.82 was paid on the original return, this amended return showed an additional tax of $6,865.17, which amount, together with interest of $411.91, was paid on March 14, 1936. The Commissioner in an audit of this return accepted this amended return as filed by the plaintiff as correct.

7. On March 14, 1936, plaintiff filed a gift-tax return for the year 1935 showing the total amount of $39,531.25 paid to the trustee of the "children's trust" and claimed no exclusions and no specific exemption. This resulted in a tax due of $4,743.75, which was paid on that same date. The Commissioner of Internal Revenue in an audit of this return accepted the return as filed by the plaintiff as correct.

8. On July 27, 1937, plaintiff filed a claim for refund of gift tax for the year 1933 in the amount of $587.50. This claim for refund was based on the contention that the gift-tax return for 1932 was incorrect and that plaintiff was entitled to eight specific exclusions of $5,000 each for that year, since in making transfers to the children's trust the plaintiff made a gift to each of his eight living grandchildren; and further that the specific credit of $50,000 was exhausted in 1932 only to the extent of $10,000. This claim alleged further that as to the year 1933 plaintiff was also entitled to eight specific exclusions of $5,000 each, which in addition to the exclusions already allowed would result in no net gifts and no tax due for that year.

When the Commissioner of Internal Revenue acted upon plaintiff's claim for refund for the year 1933, he reopened plaintiff's gift-tax liability for the year 1932 and allowed one exclusion of $5,000 on account of the transfer to the trustee of the children's trust. This allowance resulted in the Commissioner determining gross gifts for 1932 of $44,998.83 from which a specific exemption of $50,000 was allowed, leaving no taxable gifts for that year. The Commissioner also allowed plaintiff an additional exclusion of $5,000 for the year 1933 on account of the transfer to the children's trust in the

17 amount of $29,800. The Commissioner thus allowed a total of four $5,000 exclusions for the year 1933, and by carrying over from 1932 $5,001.17 of the specific exemptions of $50,000 not used in that year, he adjusted the amount of plaintiff's net taxable gifts for 1933 to the amount of $22,798.83.

As a result of the above adjustments the Commissioner determined an overassessment for 1933 in the amount of $270.07, which amount, together with interest of $31.59, was refunded to the plaintiff on October 15, 1937. In a statement attached to the certificate of over-

assessment it is stated that the plaintiff is entitled to only one $5,000 exclusion in each of the years with respect to the property placed in trust for the grandchildren, since the gifts in so far as the children are concerned are gifts of future interest against which no exclusions are allowable.

On January 17, 1938, the plaintiff was advised that his claim for refund for 1933 was rejected as to any excess over the amount allowed.

9. On July 27, 1937, the plaintiff filed a claim for refund of gift tax for the year 1934 in the amount of $7,277.08, based upon the contention that he was entitled to eight exclusions of $5,000 each on account of the transfer to the trustee for the "children's trust" and four exclusions of $5,000 each on account of the transfer to the trustee of the "adult trust," and in addition to a specific exemption in that year of $37,001.17 not consumed in prior years.

The Commissioner of Internal Revenue in acting on the claim for refund for the year 1934 allowed one exclusion for the transfer to the trustee of the "children's trust," one exclusion for the transfer to the trustee of the "adult's trust," and three exclusions for other gifts in that year, making a total of $25,000, which was $5,000 in addition to the amount claimed and allowed on the amended return. (See Finding 6 above.) As a result of these adjustments, the Commissioner reduced the amount of gifts for preceding years from $32,798.83 to $22,798.83 and disallowed the specific exemption, inasmuch as the entire specific exemption of $50,000 had been applied to gifts in the preceding years, resulting in a total tax liability for the year 1934 of $10,449.98.

18 On October 15, 1937, the Commissioner of Internal Revenue issued a certificate of overassessment to the plaintiff showing an overassessment of $1,011.25, which, together with interest of $99.73, was refunded to plaintiff on that same date. In a statement attached to this certificate of overassessment the Commissioner stated that he was disallowing the additional exclusions claimed on account of the property placed in trust for the benefit of the grandchildren for the same reason that he had disallowed it in 1933. (See Finding 8 above.)

On January 17, 1938, the plaintiff was advised that his claim for refund of gift tax for the year 1934 was rejected as to any excess over the amount allowed.

10. On July 27, 1937, the plaintiff filed a claim for refund of gift tax for the year 1935 in the amount of $4,743.74, claiming that the plaintiff was entitled to eight specific exclusions on account of the transfers made to the trustee of the "children's trust" in that year.

The Commissioner of Internal Revenue in acting on this claim for refund allowed one exclusion of $5,000 for the transfer to the trustee of the "children's trust." As a result of adjustments for preceding years, the Commissioner reduced the amount of gifts for preceding years from $222,661.83 to $207,661.83, resulting in a total tax liability for the year 1935 of $4,143.75.

On October 15, 1937, the Commissioner of Internal Revenue issued a certificate of overassessment to the plaintiff showing an overassess-

ment of $600, which, together with interest of $58.48, was refunded to the plaintiff on the same date. In a statement attached to this certificate of overassessment the Commissioner stated that he was disallowing the claim for eight specific exclusions, giving the same reason that he had given for the year 1933.

On January 17, 1938, the Commissioner of Internal Revenue notified the plaintiff by letter that the claim for refund for 1935 was rejected as to any excess over the amount allowed.

11. True copies of the two trust agreements and the certificates of overassessment to which are attached statements of the final audits made by the Bureau of Internal Revenue for each of the years 1932, 1933, 1934, and 1935 are attached to the stipulation as Exhibits A, B, C, D, and E.

19 *Conclusion of law*

Upon the foregoing special findings of fact, which are made a part of the judgment herein, the court decides as a conclusion of law that the plaintiff is entitled to recover but entry of judgment will be withheld pending submission by the parties of a computation of the amount to be included therein.

Opinion

WILLIAMS, Judge, delivered the opinion of the court:

Plaintiff seeks to recover gift taxes alleged to have been overpaid for the years 1932, 1933, 1934, and 1935. The facts have been stipulated by the parties and are not in controversy.

The plaintiff executed a trust instrument on July 14, 1932, which is herein referred to as the "children's trust." The instrument recited that it was created for the benefit of the trustor's living grandchildren (eight in number, being specifically named) and other grandchildren that might thereafter be born during the life of the trust. The instrument further provided that for a period of 10 years from the date of its execution the income from the trust fund should be accumulated and invested, that at the expiration of such ten-year period the trustee should pay an equal grandchild's distributive share of the income to each of the grandchildren who were then living and twenty-one years of age or over, and that as each grandchild reached twenty-one years of age the trustees should pay the share of the income to him. If other grandchildren were born during the life of the trust, they were entitled to participate therein on the same basis as the living grandchildren. If any of the grandchildren died leaving issue, his share should belong to his issue, but if he should die without issue his share should go to his surviving brother and/or sister, if any, and if none, then to the other grandchildren. At the termination of the trust the corpus was to be divided between the grandchildren or their survivors.

On December 28, 1934, plaintiff executed a trust instrument, herein referred to as the "adult trust." The income of this trust was to be

paid to the trustor's wife and three daughters in equal proportions.

Upon the death of the wife, her share of the income was to be
20 divided equally among the trustor's grandchildren, and upon
the death of either of the daughters her share was to go to her children in equal shares. At the termination of the trust the corpus was to go to the grandchildren of the trustor as each of them reached the age of twenty-one years.

In each of these trusts the plaintiff retained no economic interest or legal control over the property transferred, and the trustee acquired no economic interest in the property so transferred, but is charged only with the safekeeping and management of the property transferred for the benefit of the persons named. The plaintiff was powerless to change the terms of the said instruments, regain control of the property transferred, or change the interest of the beneficiaries therein. Also, the trustee is likewise powerless, and the trust instruments are self executing..

During the years 1932, 1933, 1934, and 1935, plaintiff made gifts to the children's trust, and during the year 1934 he made a gift to the trustee of the adult trust.

Plaintiff filed gift-tax returns for the years 1932, 1933, 1934, and 1935. Claims for refund for each of the years involved were duly filed and allowed in part and disallowed in part by the Commissioner of Internal Revenue. In passing on these claims the Commissioner allowed the plaintiff one $5,000 exclusion for each of the gifts to the children's trust and one $5,000 exclusion for the gift to the trustee for the adult trust. The basis of plaintiff's claim for refund and of this suit is that the plaintiff was entitled to eight $5,000 exclusions for each of the gifts for the children's trust and to four $5,000 exclusions for the gifts to the adult trust.

The question for decision is whether the taxpayer is entitled to a $5,000 exclusion in each of the years 1932, 1933, 1934, and 1935, for each of the gifts made in trust for the benefit of eight named and living grandchildren; and for the year 1934 for each of the gifts made in trust for the benefit of the taxpayer's wife and three daughters.

The Commissioner of Internal Revenue holds that in the case of the annual gifts made in trust for each of the named living grandchildren of the taxpayer only one $5,000 exclusion is allowable for each year, and that in the case of the gifts made in 1934 in trust for the taxpayer's wife and three daughters only one $5,000 exclusion is allowable.

21 Section 501 of the Revenue Act of 1932 (47 Stat. 245) provides as follows:

"(a) For the calendar year 1932 and each calendar year thereafter a tax, computed as provided in section 502, shall be imposed upon the transfer during such calendar year by any individual, resident or nonresident, of property by gift.

"(b) The tax shall apply whether the transfer is in trust or otherwise, whether the gift is direct or indirect, and whether the property

is real or personal, tangible or intangible; but, in the case of a nonresident not a citizen of the United States, shall apply to a transfer only if the property is situated within the United States. The tax shall not apply to a transfer made on or before the date of the enactment of this Act.

"(c) The tax shall not apply to a transfer of property in trust where the power to revest in the donor title to such property is vested in the donor, either alone or in conjunction with any person not having a substantial adverse interest in the disposition of such property or the income therefrom, but the relinquishment or termination of such power (other than by the donor's death) shall be considered to be a transfer by the donor by gift of the property subject to such power, and any payment of the income therefrom to a beneficiary other than the donor shall be considered to be a transfer by the donor of such income by gift."

Section 504 of the Revenue Act of 1932 (47 Stat. 247) provides as follows:

"(a) GENERAL DEFINITION.—The term "net gifts" means the total amount of gifts made during the calendar year, less the deductions provided in section 505.

"(b) GIFTS LESS THAN $5,000.—In the case of gifts (other than of future interests in property) made to any person by the donor during the calendar year, the first $5,000 of such gifts to such person shall not, for the purposes of subsection (a), be included in the total amount of gifts made during such year."

It was held by the Board of Tax Appeals in Seymour H. Knox v. Commissioner, 36 B. T. A. 630, that where the petitioner had created one trust for the benefit of two individuals he was entitled to but one exclusion, the trust being the person constituting the donee within the meaning of the statute. This decision was followed in Katherine S. Rheinstrom v. Commissioner, 37 B. T. A. 308, and was also
22 followed and the same rule announced in Edwin B. Cox v. Commissioner, 38 B. T. A. 865. In numerous other cases the Board of Tax Appeals consistently held that there could be but one $5,000 exclusion where there was but one trust indenture, no matter how many donees might be named in each trust indenture.

Recently, however, the Board in the case of Wilton Rubinstein v. Commissioner, decided January 30, 1940, reversed its position and held where property was conveyed to a trustee for the benefit of the donor's wife and three children that four exclusions of $5,000 each should be allowed, basing its decision on Welch v. Davidson, 102 Fed. (2d) 100; Robertson v. Nee, 105 Fed. (2d) 651; Rheinstrom v. Commissioner, 105 Fed. (2d) 642; and McBrier v. Commissioner, — Fed. (2d) —, (C. C. A., 3d Cir., Dec. 19, 1939), P. H. 1939, ¶ 5.756.

Welch v. Davidson, supra, was an appeal from the judgment of the federal District Court of Massachusetts, in which judgment was awarded plaintiff for gift taxes paid by the plaintiff for the calendar year 1934. In 1934 the plaintiff and his wife created an irrevocable

trust, naming the Old Colony Trust Company as trustee, in which plaintiff transferred certain property for the benefit of his seven children. The instrument provides that upon plaintiff's death the proceeds are to be divided in equal shares, one for each of the seven children of the plaintiff then surviving, and one share for the issue of any child who has died, leaving issue. The trustee is to pay the income of each share to the child for whom it is held for life, paying one-half of the principal when said child reaches the age of 45, provided that at least ten years have elapsed after the plaintiff's death. The final date of distribution is set at 21 years after the death of the survivor of the plaintiff's children and grandchildren living at the time of the establishment of the trust. The District Court, Davidson v. Welch, 22 Fed. Supp. 726, held that the donor's seven children each took a one-seventh present interest in the res of the trust created, and that the donor was entitled to a $5,000 exclusion in respect to each of them. The judgment of the District Court was affirmed.

In Rheinstrom v. Commissioner, 105 Fed. (2d) 642, the taxpayer transferred personal property to trustees for the benefit of herself and her four children. By the terms of the trust instrument
23 she retained a life interest in 40% of the entire net income.
The trustees were directed to pay to her son, Stewart H. Clifford 12½% of the entire net income. They were directed to hold 12½% of such income for the benefit of her son Benjamin B. Clifford, but with the discretion to pay over to him only so much thereof as might to them seem best, and with power to pay all or a portion thereof to his wife "and/or" children; any unexpended portion of such income to be invested for his benefit "and/or" that of his wife and children. The trustees were directed to hold 12½% of such income for the benefit of the taxpayer's son, Arthur F. Clifford, upon the same terms and conditions as were applicable to Benjamin B. Clifford. The trustees were directed to hold 12½% of such income for the benefit of the taxpayer's daughter, Katherine Clifford, with discretion to pay over only so much of the income to her as to them seemed best, and to invest any unexpended balance for her benefit. The remaining 10% of the net income was to be accumulated, invested, and held "as a reserve fund, with absolute power and discretion in said trustees to pay over to" the taxpayer "during her lifetime, such part, if any, of this 10% of the entire net income of said trust, and accumulations, if any, thereon, as may to said trustees seem best, and with absolute power and discretion in said trustees, after the death of" the taxpayer, "to pay over to the children of" the taxpayer, "or to their successors in interest as hereinafter provided, such part, if any, of this 10% of the entire net income of said trust and accumulations, if any, thereon, as may to said trustees seem best. * * *"

In her gift-tax return for the year 1934 the taxpayer excluded $20,000 by virtue of Sec. 504 (b) on the theory that she had made four gifts in creating the trust, one to each of her children, and paid her taxes upon that basis. The Commissioner of Internal Revenue,

in auditing the return, determined that the taxpayer was entitled to but one $5,000 exclusion and asserted a deficiency. The Board of Tax Appeals sustained the Commissioner's determination and in its opinion, Katherine S. Rheinstrom v. Commissioner, 37 B. T. A. 308, 312, said:

"In this case there was a gift of one corpus to one trust by virtue of one trust instrument. Although there were four benefi-
24 ciaries, there was but one transfer made by the petitioner, which was to the trust itself. We must, therefore, conclude on the authority of previous decisions that but one gift was made, and only $5,000 may be excluded."

The court, insofar as here material stated the issue as follows:

"1. Did the transfer in trust constitute one gift to the trust or four gifts to the beneficiaries?

"2. If it constituted four gifts, were three of them gifts of 'future interests'?"

After a thorough consideration and discussion of the cases cited by both the plaintiff and the defendant, the court said, p. 647:

"It is our conclusion that the taxpayer, in creating this trust, made four gifts—one to each of her children—and that she made no gift or gifts to the trust or to the trustees.

"2. The Commissioner contends, however, that, even if this is so, it would make no difference in the taxpayer's gift tax liability, since only her son Stewart received an unconditional present vested interest in his share of the income of the trust estate, and the interests of the other three children are to be regarded as 'future interests.' The Commissioner directs attention to the fact that by the terms of the trust instrument the trustees are not required to pay to these three children their proportion of the income, but may accumulate it for their benefit, or, in the case of two of them, may pay it to them, their wives or children. It is true that the three children, other than Stewart, received no unconditional right to have their shares of the income paid to them by the trustees. It is equally true, however, that the taxpayer retained no interest in the shares of income which were assigned to them, and that, by the terms of the trust, each of them (or the wives and children of the two sons) were to have his or her share or it was to be accumulated for his or her benefit. The enjoyment of the benefits conferred upon three of her children by the taxpayer was conditional, but it was to commence at once and not at some future date and was for their sole and immediate benefit.

* * * * * * *

"The Commissioner cites no case which sustains his position that the interests donated by the taxpayer to, or for the benefit of, three of her children, were future interests, and we think that they were not.

* * * * * * *

25 "The decision of the Board is affirmed insofar as it holds that the taxpayer retained a life interest in only 40 percent of the income from the trust estate. It is reversed insofar as it holds that

the taxpayer was entitled to one exclusion for one gift, instead of four exclusions for four gifts. The case is remanded to the Board for a redetermination of the deficiency in accordance with this opinion."

In Commissioner v. Wells, 88 Fed. (2d) 339, it was held that the beneficiary of a trust which provided for the accumulation of income until he became of age, when he was to receive the income until he was 30, or until the death of his mother, when he was to receive the corpus, was not a gift of future interest, mainly upon the ground that it was the interest transferred by the taxpayer, and not that received by the beneficiary, which determined whether the gift was of a present or a future interest.

In Commissioner v. Krebs, 90 Fed. (2d) 880, the court dealt with trusts which directed the trustees to use the income from the trust estate for the support, maintenance, benefit, and education of named beneficiaries until they were 25 years of age, the unexpended income to be then paid to them or their issue, appointees, or distributees. It was held that the gifts, whether regarded as being to the trust or to the beneficiaries, were not gifts of "future interests."

In Noyes v. Hassett, 20 Fed. Supp. 31, the District Court of Massachusetts ruled that under a trust which permitted the trustees to accumulate income for the beneficiaries and to pay it to them or their guardians, or for the use or benefit of the beneficiaries, with discretion in the trustees to determine what expenditures were for the use or benefit of the beneficiaries, the gifts were not of future interests.

Thus it appears from the decided cases that the courts have rejected the contentions made by the defendant in this case. It is therefore held:

(1) That the gifts set up by plaintiff in the two trusts involved were of present interests in the property transferred, and

(2) That each beneficiary named in the respective trust instruments is a donee within the provisions of section 504 (b) of the gift-
26 taxing statute of 1932, for each of whom plaintiff is entitled to an exclusion of $5,000 in the computation of the net amount of gifts subject to the tax in each of the years involved.

Plaintiff is entitled to recover. The entry of judgment, however, will be suspended pending the filing of a stipulation by the parties showing the exact amount of the judgment to be awarded plaintiff, computed in accordance with the opinion of the court. It is so ordered.

WHITAKER, Judge; GREEN, Judge; and WHALEY, Chief Justice, concur.

LITTLETON, Judge, took no part in the decision of this case.

28 *V. Judgment*

At a Court of Claims held in the City of Washington on June 3, 1940, the court filed the following order entering judgment for plaintiff:

This case comes before the court on plaintiff's motion for the entry of judgment in accordance with the stipulation of the parties filed herein April 22, 1940, in which stipulation certain sums are mentioned as due plaintiff based on the special findings and opinion of the court filed March 4, 1940; and in accordance with said stipulation it is ordered this 3rd day of June 1940, that the plaintiff's motion for the entry of judgment be and the same is allowed, and judgment is now entered in favor of plaintiff in the sum of ten thousand, seven hundred twenty-seven dollars and one cent ($10,727.01), $317.43, a part thereof, to bear interest at the rate of six percent per annum from November 27, 1935; $6,265.83, a part thereof, to bear interest at the rate of six percent per annum from March 17, 1936, and the balance thereof, $4,143.75, to bear interest at the rate of six percent per annum from March 24, 1936, all according to law.

30 [Clerk's certificate to foregoing transcript omitted in printing.]

[Endorsement on cover:] Enter Attorney General. File No. 44742. Court of Claims. Term No. 393. The United States, Petitioner, vs. Arthur Pelzer. Petition for writ of certiorari and exhibit thereto. Filed September 3, 1940. Term No. 393 O. T. 1940.

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Supreme Court of the United States

Order allowing certiorari

Filed October 21, 1940

The petition herein for a writ of certiorari to the Court of Claims is granted. And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

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U. S. GOVERNMENT PRINTING OFFICE 1940

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FILE COPY

No. 393

In the Supreme Court of the United States

October Term, 1940

The United States, petitioner,

v.

Arthur Pelzer

PETITION FOR A WRIT OF CERTIORARI TO THE COURT OF CLAIMS

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INDEX

CITATIONS

256786—40

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In the Supreme Court of the United States

October Term, 1940

No. —

The United States, petitioner

v.

Arthur Pelzer

PETITION FOR A WRIT OF CERTIORARI TO THE COURT OF CLAIMS

The Solicitor General, on behalf of the United States, prays that a writ of certiorari issue to review the judgment of the Court of Claims entered in the above-entitled cause on June 3, 1940.

OPINION BELOW

The opinion of the Court of Claims (R. 19–26) is reported in 31 F. Supp. 770.

JURISDICTION

The judgment of the Court of Claims was entered June 3, 1940. (R. 28.) The jurisdiction of this Court is invoked under Section 3 (b) of the Act of February 13, 1925, as amended by the Act of May 22, 1939.

QUESTIONS PRESENTED

1. Whether the donor of a gift in trust is entitled under the provisions of Section 504 (b) of the Revenue Act of 1932 to one $5,000 exclusion for the entire trust or to a separate $5,000 exclusion for each of the beneficiaries of the trust.

2. If the number of such exclusions is to be determined by the number of beneficiaries, whether gifts in trust in which the rights of the beneficiaries to possession and enjoyment are postponed for a period of years constitute gifts of "future interests in property" for which no exclusions are allowable under Section 504 (b).

STATUTE AND REGULATIONS INVOLVED

Revenue Act of 1932, c. 209, 47 Stat. 169:

> SEC. 501. IMPOSITION OF TAX.
>
> (a) For the calendar year 1932 and each calendar year thereafter a tax, computed as provided in section 502, shall be imposed upon the transfer during such calendar year by any individual, resident or nonresident, of property by gift.
>
> (b) The tax shall apply whether the transfer is in trust or otherwise, whether the gift is direct or indirect, and whether the property is real or personal, tangible or intangible; but, in the case of a nonresident not a citizen of the United States, shall apply to a transfer only if the property is situated within the United States. The tax shall not apply to a transfer made on or before the date of the enactment of this Act. (U. S. C., Title 26, Sec. 550.)
>
> * * * * *

SEC. 504. NET GIFTS.

(a) *General Definition.*—The term "net gifts" means the total amount of gifts made during the calendar year, less the deductions provided in section 505.

(b) *Gifts Less Than $5,000.*—In the case of gifts (other than of future interests in property) made to any person by the donor during the calendar year, the first $5,000 of such gifts to such person shall not, for the purposes of subsection (a), be included in the total amount of gifts made during such year. (U. S. C., Title 26, Sec. 553.)

* * * * *

SEC. 1111. DEFINITIONS.

(a) When used in this Act—

(1) The term "person" means an individual, a trust or estate, a partnership, or a corporation. (U. S. C., Title 26, Sec. 1696.)

* * * * *

Treasury Regulations 79, promulgated under the Revenue Act of 1932:

ART. 11. *Future interests in property.*—The gift of a future interest in property, regardless of the amount thereof, is to be included in determining the total amount of gifts made during any calendar year. A future interest in property is any interest or estate in property, whether vested or contingent, which is limited to commence in use, possession, or enjoyment at some future date or time. Gifts of such interests are taxable subject only to the deductions authorized

by section 505. For the valuation of future interests, see article 19.

* * * * *

STATEMENT

The special findings of fact of the Court of Claims (R. 10–18) may be summarized as follows:

On July 14, 1932, respondent executed a trust instrument for the benefit of his then living grandchildren (eight in number being specifically named) and any other grandchildren that might thereafter be born during the life of the trust. The instrument provided that for a period of ten years from the date of its execution, the income from the trust was to be accumulated, that at the expiration of the ten-year period the trustee was to pay an equal share of the income to each of the grandchildren who were then living and twenty-one years of age or over, and as each grandchild reached twenty-one years of age thereafter the trustee was to pay his share of the income to him. Any other grandchildren born during the life of the trust were to participate therein on the same basis as the eight living grandchildren, and the share of any deceased grandchild was to go to his issue, if any, or in the absence of such issue, to his surviving brother and/or sister, if any, and if none, then to the other grandchildren. The trust was to continue and the income to be distributed until twenty-one years after the death of the last survivor of the eight living grandchildren, at which time the corpus was to be divided among any other then living grandchil-

dren and the issue of all deceased grandchildren *per stirpes.* (R. 10–12.)

On December 28, 1934, respondent executed another trust instrument for the benefit of his wife and three daughters. The income of this trust was to be paid to the four beneficiaries in equal proportions. Upon the death of the wife, her share of the income was to be divided equally among the respondent's grandchildren, and upon the death of any of the daughters, her share of the income was to be divided equally among her children. On reaching the age of twenty-two, each grandchild was to receive his share of the corpus of his grandmother's portion, if the grandmother was then deceased, or upon her decease thereafter, and his share of his mother's portion, if his mother was then deceased, or upon her decease thereafter. (R. 13–15.)

During the years 1932, 1933, 1934 and 1935 respondent made gifts to the first trust, and during the year 1934 to the second trust. In addition, respondent made other gifts in the taxable years to individual donees. (R. 13, 15, 16.)

Respondent duly filed gift tax returns for the years 1932, 1933, 1934 and 1935. No question of tax liability for the year 1932 is presented, since the total net gifts in that year was less than the $50,000 specific exemption. The Commissioner of Internal Revenue found a deficiency and assessed an additional tax for the year 1933 which was duly paid. He accepted as correct the returns filed for the

years 1934 and 1935. The respondent thereafter filed claims for refund for the years 1933, 1934 and 1935 based upon the theory that he was entitled to eight $5,000 exclusions for each of the gifts to the first trust and to four such exclusions for the gifts to the second trust. These claims were allowed in part by the Commissioner on the basis of a computation permitting one $5,000 exclusion for each of the gifts to the first trust, and one $5,000 exclusion for each of the gifts to the second trust, in addition to the exclusions for the gifts to the individual donees. (R. 16–18.)

In the Court of Claims the Government contended (1) that the trusts and not the beneficiaries were the donees of the gifts and, accordingly, only one exclusion was allowable for each gift to each trust, but that (2) if the beneficiaries were to be regarded as the donees, then the beneficiaries of the first trust received future interests within the meaning of Section 504 (b) of the Revenue Act of 1932, *supra,* for which no exclusions were allowable. The Court of Claims held (1) that the gifts set up in both trusts were of present interests, and (2) that each beneficiary named was a donee within the provisions of Section 504 (b), for each of whom the respondent was entitled to an exclusion of $5,000. (R. 25–26.)

SPECIFICATION OF ERRORS TO BE URGED

The Court of Claims erred:

1. In holding that under Section 504 (b) of the Revenue Act of 1932 respondent was entitled to

an exclusion of $5,000 for each beneficiary of the trusts in the computation of the net amount of gifts to the trusts subject to tax in each of the years involved.

2. In holding that gifts to a trust, the income of which is to be accumulated for ten years before any payments are to be made to the beneficiaries, are gifts of present interests in the property transferred.

3. In failing to enter judgment for the United States and to dismiss the petition.

REASONS FOR GRANTING THE WRIT

The decision of the Court of Claims that the beneficiaries and not the trust are the donees and that therefore a $5,000 exclusion is available for each beneficiary is in direct conflict with the decision of the Circuit Court of Appeals for the Seventh Circuit in *United States* v. *Ryerson*, decided July 9, 1940, not yet officially reported but found in 1940 C. C. H., Vol. 4, par. 9576.[1] The court there held that, under Section 504 (b) of the Revenue Act of 1932, the trust is the donee and therefore only one exclusion per trust is available regardless of the number of beneficiaries.

---

[1] The following decisions, in accord with the decision below, are likewise in conflict with the *Ryerson* case: *Welch* v. *Davidson*, 102 F. (2d) 100 (C. C. A. 1st); *Rheinstrom* v. *Commissioner*, 105 F. (2d) 642 (C. C. A. 8th); *Robertson* v. *Nee*, 105 F. (2d) 651 (C. C. A. 8th); *McBrier* v. *Commissioner*, 108 F. (2d) 967 (C. C. A. 3d); *Hutchings* v. *Commissioner*, 111 F. (2d) 229 (C. C. A. 5th); *Early* v. *Reid* (C. C. A. 4th), decided August 7, 1940, not yet officially reported but found in 1940 C. C. H., Vol. 4, par. 9634.

The *Ryerson* case was based squarely on the earlier decision of the same court in *Commissioner v. Wells*, 88 F. (2d) 339, which held that a gift to a trust, the beneficial enjoyment of which was to commence *in futuro*, was not the gift of a future interest because, for purposes of Section 504 (b), the person to whom the gift was made was the trust and not the beneficiary. Having fixed upon the trust as the donee for purposes of the "future interest" question presented in the *Wells* case, the court consistently held that the trust was the donee for purposes of the "exclusion" question presented in the *Ryerson* case.

The *Wells* and *Ryerson* decisions illustrate the close relationship between the two questions involved in the present case. If, as the court below held, the beneficiaries are to be treated as the donees for the purpose of determining the number of exclusions allowable, then it must be the character of their interest which determines whether the gift was of a present or of a future interest. Here the grandchildren, as beneficiaries of the first trust, were to receive no payment for at least ten years; if they are to be regarded as the donees, it seems plain that the interests they acquired were future interests and that, therefore, the respondent is entitled to no exclusions with respect to the gifts to them. If, on the other hand, as the court held in the *Ryerson* case, the trust is the donee for purposes of Section 504 (b), the gifts were clearly of

a present interest, but only one $5,000 exclusion was allowable with respect to each trust.

The questions presented are of considerable importance. There are at the present time in various stages of litigation before the federal courts approximately 35 cases in which the problem is involved. In one of these, *Hutchings* v. *Commissioner,* 111 F. (2d) 229 (C. C. A. 5th), this Court has granted an extension of time within which to file a petition for certiorari. In addition, a considerably larger number of cases are pending before the Board of Tax Appeals and in the Bureau of Internal Revenue.

While Section 505 of the Revenue Act of 1938, c. 289, 52 Stat. 447, withdraws the exclusion in the case of gifts to trusts made on or after January 1, 1939, the amount of tax on gifts made after that date by a donor who made gifts in trust before 1939 will continue to be affected; this is so because, under Section 502 of the 1932 Act, which has not been changed in this respect by subsequent acts, the rate of tax on gifts made each year depends in part upon the aggregate amount of the net gifts made by the taxpayer in preceding years. The Gift Tax Section of the Miscellaneous Tax Unit of the Bureau of Internal Revenue estimates that of the approximately 25,000 gift tax returns filed during the years 1932 to 1938, about one-third involved gifts by trust. It is apparent, therefore, that despite the 1938 Act, the problem will constantly recur unless finally settled by this Court.

CONCLUSION

The decision below is in direct conflict with the decision in the *Ryerson* case, and the questions are of general importance. Therefore, we respectfully submit that this petition for a writ of certiorari should be granted.

FRANCIS BIDDLE,
Solicitor General.

SEPTEMBER, 1940.

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FILE COPY

No. 393

In the Supreme Court of the United States

October Term, 1946

The United States, Petitioner

v.

[illegible]

On writ of certiorari to the [illegible]

BRIEF FOR THE UNITED STATES

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INDEX

CITATIONS

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In the Supreme Court of the United States

OCTOBER TERM, 1940

No. 393

THE UNITED STATES, PETITIONER

v.

ARTHUR PELZER

ON WRIT OF CERTIORARI TO THE COURT OF CLAIMS

BRIEF FOR THE UNITED STATES

OPINION BELOW

The opinion of the Court of Claims (R. 11–16) is reported in 31 F. Supp. 770.

JURISDICTION

The judgment of the court below was entered June 3, 1940 (R. 16–17). The petition for a writ of certiorari was filed September 3, 1940 (R. 17), and was granted October 21, 1940. The jurisdiction of this Court is invoked under Section 3 (b) of the Act of February 13, 1925, as amended by the Act of May 22, 1939.

QUESTIONS PRESENTED

1. Whether under Section 504 (b) of the Revenue Act of 1932 the donor of a gift in trust is entitled to one $5,000 exclusion for the entire trust or to a separate $5,000 exclusion for each of the beneficiaries of the trust.

2. If the number of exclusions is to be determined by the number of beneficiaries, whether certain gifts in trust were of "future interests in property" for which no exclusions are allowable under Section 504 (b).

STATUTES AND REGULATIONS INVOLVED

The pertinent provisions of the Revenue Acts of 1932 and 1938 and of the treasury regulations promulgated thereunder are set out in the Appendix.

STATEMENT

The special findings of fact of the Court of Claims (R. 4–11) may be summarized as follows:

On July 14, 1932, the taxpayer created a trust, hereafter referred to as the 1932 trust, for the benefit of his then living grandchildren (eight in number being specifically named in the trust instrument) and any other grandchildren that might thereafter be born during the life of the trust. The trust instrument provided that for a period of ten years from the date of its execution the net income from the trust estate should be accumulated and invested and reinvested; that upon the expiration

of the ten-year period the trustee should thereafter pay an "equal grandchild's distributive share" of the income to each of the grandchildren named in the trust who were then living and twenty-one years of age or over, such payments to continue to each during his life; that as and when each of the remaining grandchildren named in the trust reached twenty-one years of age the trustee should thereafter pay to him for and during his life "an equal grandchild's distributive share" of the income; but that during the respective minorities of the grandchildren named in the trust all net income not required to be paid out by the terms of the trust to adult named grandchildren or to grandchildren born subsequent to the execution of the trust instrument should be accumulated. The trust instrument also provided that any other grandchildren born during the life of the trust should participate therein on the same basis as the eight named grandchildren, except as to distributions of income made prior to the birth of the thereafter born grandchildren, and except that the thereafter born grandchildren should be paid their shares of the income during their respective minorities after the initial ten-year accumulation period. The trust instrument further provided that the distributive share of the net income of any deceased grandchild was to go to his issue *per stirpes,* if any, and, in the absence of such issue, to his surviving brother and/or sister, if any, and, if none, then to the other

grandchildren *per stirpes,* subject in any event to the terms of the trust. Finally, the trust instrument provided that the trust should continue and the income therefrom be distributed as provided until twenty-one years after the death of the last survivor of the eight named living grandchildren, at which time the trust should cease and the corpus should be divided among any then living grandchildren and the issue of all deceased grandchildren, the issue of a deceased grandchild to receive the deceased parent's share, *per stirpes* (R. 4–6).

On December 28, 1934, the taxpayer created a second trust, hereafter referred to as the 1934 trust, for the benefit of his wife and three daughters. The trust instrument provided that the income of this trust should be paid to the four beneficiaries in equal proportions, that upon the death of the wife, her share of the income should be divided equally among all of the taxpayer's grandchildren; that upon the death of any of the daughters, her share of the income should go to her children in equal shares, and that on the death of any grandchild leaving issue such grandchild's share should go to such issue, and if no issue to such grandchild's heirs at law. The trust instrument further provided that on reaching the age of twenty-two, each grandchild should receive free of the trust his share of his grandmother's (i. e. the taxpayer's wife's) portion of the corpus, if the grandmother was then deceased, or upon her decease thereafter,

and his share of his mother's portion, if his mother was then deceased, or upon her decease thereafter. In the event of the death of a daughter leaving no issue, the trust instrument provided that her share of the corpus should go to her heirs at law. (R. 7–8.)

During the years 1932, 1933, 1934, and 1935 the taxpayer made gifts to the first, or 1932, trust. During the year 1934 the taxpayer made gifts to the second, or 1934, trust and other gifts directly to his three daughters who were beneficiaries of the 1934 trust. (R. 6–9.)

The taxpayer duly filed gift tax returns for the years 1932, 1933, 1934, and 1935. No question of tax liability for the year 1932 was or is presented, since the total net gifts in that year were less than the $50,000 specific exemption. The Commissioner of Internal Revenue found a deficiency and assessed an additional tax for the year 1933 which was duly paid. He accepted as correct the returns filed for the years 1934 and 1935. During this period the Commissioner evidently was proceeding on the theory, in which the taxpayer concurred, that the beneficiaries of the trusts were the "persons" to whom the gifts were made, with the results that four exclusions were allowable annually from gifts to the 1934 trust, but that no exclusions were allowable from gifts to the 1932 trust, because the beneficiaries of that trust took only future interests. (R. 6–9.)

Thereafter, in July 1937, the taxpayer filed claims for refund for the years 1933, 1934, and 1935, based upon the theory that he was entitled to eight \$5,000 exclusions annually from gifts to the 1932 trust, to four exclusions from gifts in 1934 to the 1934 trust, and to three exclusions from gifts made in 1934 directly to beneficiaries of the 1934 trust. (R. 2–4, 9–10.) These claims were allowed in part by the Commissioner. Operating on the theory that the trusts were the "persons" to whom the gifts were made, he allowed one \$5,000 exclusion annually from gifts to the 1932 trust and one \$5,000 exclusion from gifts to the 1934 trust, as well as three exclusions from gifts made directly to the beneficiaries of the 1934 trust. (R. 8–11.) In his certificates of overassessment the Commissioner explained that the gifts to the 1932 trust were, insofar as the beneficiaries were concerned, of future interests from which no exclusions were allowable. (R. 9–11.)

In the court below the Government contended (1) that the trusts and not the beneficiaries were the donees of the gifts, with the result that only one exclusion was allowable annually from gifts to each trust, but that (2) if the beneficiaries were to be regarded as the donees, then the beneficiaries of the 1932 trust received future interests within the meaning of Section 504 (b) of the Revenue Act of 1932, from which no exclusions were allowable. The Court of Claims held (1) that the gifts in trust

were of present interests, and (2) that each beneficiary named in the respective trust instruments is a donee within the provisions of Section 504 (b), for each of whom the taxpayer is entitled to an exclusion of $5,000 in the computation of the net amount of gifts subject to tax. (R. 16.)

SPECIFICATION OF ERRORS TO BE URGED

The Court of Claims erred:

1. In holding that under Section 504 (b) of the Revenue Act of 1932 the taxpayer is entitled to a separate $5,000 exclusion for each of the beneficiaries of the trusts.

2. In holding that the gifts in trust under the 1932 trust were gifts of present interests in the property transferred.

3. In entering judgment against the United States and in failing to enter judgment for the United States and to dismiss the petition.

SUMMARY OF ARGUMENT

I. Section 504 (b) of the Revenue Act of 1932 excludes from the gift tax the first $5,000 of gifts, other than of future interests in property, "made to any person" by the donor during the year. Under this provision the donor of gifts in trust may take only one $5,000 exclusion from gifts to a single trust, regardless of the number of the beneficiaries of the trust, for the trust is the "person" to which the gifts are made. Section 1111 (a) (1) defines "person" as including "a trust"; a trust

is regularly treated for tax purposes as an entity composed of but distinct from the trustee and the beneficiaries; and a gift in trust is technically made to the trust entity. Further, the rule that under Section 504 (b) the trust is the donee of gifts in trust, and not the beneficiaries, is administratively expedient. It avoids, in the case of gifts in trust, the necessity which would otherwise exist of determining the number and identity of the beneficiaries and the nature and value of their separate interests in each gift. These determinations would frequently be difficult, and that as to value virtually impossible.

II. Gifts "of future interests in property" are excepted from the $5,000 exclusion from the gift tax provided by Section 504 (b). If, as we contend, the trust is the "person" to which a gift in trust is given, there arises no question whether the gifts in this case were of future interests, for the trusts, as entities, took present interests. But if that contention is rejected, and the beneficiaries are held to be the donees, we contend that the beneficiaries of the 1932 trust received only future interests in the gifts to that trust. Under the 1932 trust instrument the income was to be accumulated for ten years, and then was to be paid over in equal shares to the donor's grandchildren or to designated representatives of deceased grandchildren. The reports of the congressional committees state that "future interests in property" in Section 504 (b)

refers to any interest "limited to commence in possession or enjoyment at a future date." The Treasury regulations, tacitly approved by Congress by reenactment of the statute, use substantially the same language. Here there can be no doubt that the interests of the beneficiaries were not to commence in possession or enjoyment until at least ten years after the creation of the trust. Further, the committee reports state that by excepting gifts of future interests from the exclusion they sought to avoid the "apprehended difficulty * * * of determining the number of eventual donees and the values of their respective gifts." These determinations can be avoided in this case, and as to all gifts in trust, by considering the trust as the donee, as urged in point I. But Congress, by excepting from the exclusion gifts of future interests, intended to eliminate these questions as to direct gifts too. Various lower court decisions, while not as clearly involving future interests as does the case at bar, fail to give proper effect to this plainly expressed intent of Congress.

ARGUMENT

Introductory; administrative construction, lower court decisions.—Section 501 of the Revenue Act of 1932 imposes a tax on the transfer of property by gift. Section 502 prescribes the method for computing the gift tax at enumerated rates "on the aggregate sum of the net gifts." Section 504 (a)

defines "net gifts" as the total amount of gifts made during the calendar year, less certain deductions. Finally Section 504 (b), with which we are here concerned, provides that—

> In the case of gifts (other than of future interests in property) made to any person by the donor during the calendar year, the first $5,000 of such gifts to such person shall not, for the purposes of subsection (a), be included in the total amount of gifts made during such year.

Section 504 (b) thus excludes from the gift tax the first $5,000 of gifts "made to any person" by the donor during the year, except that this exclusion does not apply to gifts "of future interests in property." In the present case the taxpayer made transfers of property in trust, the income therefrom to be paid to his grandchildren after an initial accumulation period of ten years. This and similar gifts in trust raise two questions under Section 504 (b). The first is whether the donor is entitled to one $5,000 exclusion for the entire trust, or to a separate $5,000 exclusion for each of the beneficiaries of the trust. More accurately, whether the donor may exclude only the first $5,000 of gifts to the trust, or whether he may treat the gifts as made to the beneficiaries, and exclude $5,000 from the gifts to each beneficiary. This turns on whether for purposes of Section 504 (b) the "person" to whom the gift is made is the trust as a separate legal entity or the beneficiaries. The second question

raised is whether the gifts are of "future interests in property," from which no exclusions are allowed by Section 504 (b).

These two questions are interconnected, and have been so treated by the administrative officers and the lower Federal courts. If under Section 504 (b) the "person" to whom the gift is made is the trust and not the beneficiaries, so that only one $5,000 exclusion is allowable, the gift is of a present and not of a future interest, for the trust receives a present interest. If, on the other hand, the beneficiaries are to be treated as the donees for the purpose of determining the number of exclusions allowable, then it is the characters of their interests which determine whether or to what extent the gift was of a present or of a future interest. Here, for example, the grandchildren, as beneficiaries of the 1932 trust, were to receive no payments for at least ten years; if they are to be regarded as the donees we think that the gifts to them were of future interests and that, therefore, the taxpayer was entitled to no exclusions from those gifts. The court below, however, not only held that the beneficiaries were the donees for determining the number of exclusions but that they received present and not future interests. We contest both points here, the first primarily, the second alternatively if the first be determined against us.

In administering the gift tax the Treasury proceeded for some years on the assumption that

under Section 504 (b) the beneficiaries of a gift in trust were to be considered as the donees, rather than the trust as a separate entity. Under this practice an exclusion of $5,000 was allowed for each beneficiary from gifts of present interests in property. As a corollary, the Treasury took the position during this period that whether a gift in trust was of a present or of a future interest was determinable by the character of the interest of the beneficiaries. This construction of the act was not lucidly articulated in the regulations, but it plainly was tacitly assumed therein. See Regulations 79, 1933 edition, Article 11, paragraph 2; 1936 edition, Article 21, both set out in the Appendix, *infra*. In the present case the initial administrative view that the beneficiaries of a gift in trust were the donees, and that the character of their interest was to be looked to to determine whether the gift was of a future interest, was reflected in the Commissioner's first audits of the taxpayers' returns for 1933, 1934, and 1935. Thus he allowed one $5,000 exclusion for each of the beneficiaries of the 1934 trust, but refused to allow any exclusion from gifts to the 1932 trust, unquestionably on the theory that the gifts to the beneficiaries of the 1932 trust were of future interests. (See R. 6–9.)

In 1938, however, the Bureau altered its construction of Section 504 (b) as a result of the decisions in *Wells* v. *Commissioner*, 34 B. T. A. 315

(1936), affirmed *sub nom. Commissioner* v. *Wells,* 88 F. (2d) 339 (C. C. A. 7th, 1937); *Commissioner* v. *Krebs,* 90 F. (2d) 880 (C. C. A. 3d) (1937); and *Knox* v. *Commissioner,* 36 B. T. A. 630 (1937). In the *Wells* case the taxpayer created three trusts, one for each of his children, the trust instruments providing that the income should be accumulated for a certain period and thereafter be distributed to the beneficiaries. The Commissioner refused to allow exclusions from gifts to these trusts on the ground that the gifts were of future interests. The Board held for the taxpayer. 34 B. T. A. 315. As an alternate ground of decision, it said that "the character of the interest that the donee takes" (p. 317) was decisive of whether the gift was of a future interest, that the trusts as entities might properly be regarded as the donees, and that the trusts took present interests in the property. On appeal by the Commissioner, the Circuit Court of Appeals for the Seventh Circuit affirmed, upon the theory that the trusts, which took present interests, were the donees, rather than the ultimate beneficiaries. 88 F. (2d) 339. Agreement with this view was expressed by the Circuit Court of Appeals for the Third Circuit in *Commissioner* v. *Krebs,* 90 F. (2d) 880 (1937); see also *Noyes* v. *Hassett,* 20 F. Supp. 31 (D. Mass., 1937).

In the *Wells* case there were as many trusts as beneficiaries, and hence no question was presented as to the number of $5,000 exclusions. The theory

adopted there and in the *Krebs* case, that the trusts were the donees, required, however, as a matter of logical consistency, that the number of exclusions be determined by the number of trusts rather than by the number of beneficiaries. In the *Krebs* case, indeed, one $5,000 exclusion was allowed from gifts to each of six trusts having but three beneficiaries altogether, although it is not clear to what extent this feature of the case was considered by the court. At any rate, in the *Knox* case (36 B. T. A. 630, 633), the Board of Tax Appeals held, on the authority of the *Wells* and *Krebs* cases, that the number of exclusions was to be determined by the number of trusts rather than by the number of beneficiaries, where the latter outnumbered the former.

Thereupon, in 1938, the Bureau changed its construction of the act and acquiesced in these decisions. It withdrew its prior nonacquiescence in the decision of the Board in the *Wells* case (Cum. Bull. XV–1, p. 48 (1936)), and acquiesced in that decision (Cum. Bull. 1938–1, p. 32) [1] and in the decision of the Board in the *Knox* case (Cum. Bull. 1938–1, p. 17). And it published the decisions of the circuit courts of appeals in the *Wells* and *Krebs* cases. Ct. D. 1310, Cum. Bull. 1938–1, p.

[1] The issue of the cumulative bulletin containing the acquiescence and withdrawal of prior nonacquiescence in the *Wells* decision repeats elsewhere the nonacquiescence in that decision. Cum. Bull. 1938–1, p. 60. Undoubtedly this repetition was an oversight.

516, and Ct. D. 1311, Cum. Bull. 1938–1, p. 518.[2] This metamorphosis in the administrative construction is also reflected in this case. The taxpayer filed claims for refunds, and in auditing them the Commissioner, altering his prior practice, allowed a $5,000 exclusion annually from gifts to the 1932 trust, although he expressed continued adherence to the view that the gifts, so far as the beneficiaries were concerned, were of future interests. (R. 9–10.) This changed construction resulted in substantial refunds to the taxpayer here (R. 9, 10, 11); undoubtedly innumerable refunds were made and innumerable exclusions allowed in other similar cases.

Moreover, this construction of the Act, that the trust entity is the donee of a gift in trust and not the beneficiaries, enabled donors to avoid gift taxes by creating a number of trusts for one person and claiming an exclusion for each trust. See *Cox* v. *Commissioner,* 38 B. T. A. 865

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[2] Although the Bureau thus published its acquiescence in the *Wells* and *Knox* decisions, and actually altered its former practice, it never issued any ruling explaining the change, and the Treasury regulations tacitly embodying the earlier view were never repudiated or amended retroactively. In 1938, however, the regulations were amended to conform them to the 1938 amendments of the gift-tax provisions of the 1932 Act. See T. D. 4830, Cum. Bull. 1938–2, p. 368. And in this amendment the provisions of the regulations reflecting the earlier view, that the beneficiaries are the donees of gifts in trust, were omitted. Compare sentence 1 of Article 21 of Regulations 79, 1936 edition, with sentence 1 of Article 21 of Regulations 79, 1936 edition as amended in 1938, both set out in the Appendix, *infra*, pp. 45–47.

(1938); *McBrier* v. *Commissioner*, 108 F. (2d) 967, 968, 969 (C. C. A. 3d). To shut this loophole Section 504 (b) of the 1932 Act was amended by Section 505 of the Revenue Act of 1938 (set out *infra* p. 41) to allow no exclusion at all from gifts in trust.[3] This amendment was prospective only; it applies only to 1939 and subsequent years.

Thereafter, however, when the Commissioner sought, in turn, to invoke the construction that the trust is the donee, for the purpose of determining the number of exclusions, many of the lower federal courts, and eventually the Board of Tax Appeals, repudiated the *Wells, Krebs,* and *Knox* decisions and held that the taxpayers were entitled to as many exclusions as there were beneficiaries receiving present interests. *Welch* v. *Davidson,* 102

[3] The Senate Finance Committee, with which the amendment originated, stated (S. Rep. No. 1567, 75th Cong., 3d Sess., p. 41):

"The committee is also proposing an amendment by which the exclusion would not apply to gifts in trust. The Board of Tax Appeals and several of the Federal courts have held, with respect to gifts in trust, that the trust entities were the donees and on that account the gifts were of present and not of future interests. The statute, as thus construed, affords ready means of tax avoidance, since a donor may create any number of trusts in the same year in favor of the same beneficiary with a $5,000 exclusion applying to each trust, whereas the gifts, if made otherwise than in trust, would in no case be subject to more than a single exclusion of $5,000. The proposed change does not reduce the $40,000 specific exemption for gifts. The amendment will apply only when computing the tax for the calendar year 1939 and succeeding calendar years."

F. (2d) 100 (C. C. A. 1st); *Rheinstrom* v. *Commissioner*, 105 F. (2d) 642 (C. C. A. 8th); *Robertson* v. *Nee*, 105 F. (2d) 651 (C. C. A. 8th); *McBrier* v. *Commissioner*, 108 F. (2d) 967 (C. C. A. 3d); *Hutchings* v. *Commissioner*, 111 F. (2d) 229 (C. C. A. 5th), certiorari granted, No. 419 this Term, to be argued herewith; *Early* v. *Reid* (C. C. A. 4th), decided August 7, 1940, not yet reported but found in 1940 C. C. H., Vol. 4, par. 9634, pending on petition for certiorari No. 556, this Term; *Rubinstein* v. *Commissioner*, 41 B. T. A. 220.[4] The Seventh Circuit alone adhered to the earlier view. In *United States* v. *Ryerson*, 114 F. (2d) 150, certiorari granted, No. 495 this Term, to be argued herewith, it held that the trust was the donee for the purpose of determining the number of exclusions. This, it said, was the plain implication of its reasoning in the *Wells* case. See 114 F. (2d) at 155.

Although these holdings that the beneficiaries were the donees for the purpose of determining the number of exclusions made necessary the conclusion that it was the interest received by the beneficiary which determined whether the gift was of a future interest, the same courts, as shown in detail in point II hereof, gave to the term "future inter-

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[4] In the *McBrier* case the Third Circuit distinguished its earlier decision in the *Krebs* case as *dicta*. In the *Rubinstein* case the Board of Tax Appeals specifically overruled its earlier decisions.

est" a very narrow construction, and held for the taxpayer without exception.

The final result of the court decisions is well stated by Judge Woodrough, dissenting in *Rheinstrom* v. *Commissioner,* 105 F. (2d) 642, 648 (C. C. A. 8th):

> It seems to me that the gift tax exemption clause, 26 U. S. C. A. § 553, has been learnedly interpreted too much. The interpretations are in diametrical conflict, but join in defeating the tax assessor. * * *

The primary position of the Government in this case is that only one exclusion of $5,000 is allowable annually from gifts to any one trust, regardless of the number of beneficiaries of the trust. If this contention is rejected, whether the gifts are of future interests must be determined by the nature of the interests bestowed on the beneficiaries, and, as a secondary defense, we think it quite clear that the beneficiaries of the 1932 trust received future interests as that term is used in the statute.

I

ONLY ONE EXCLUSION IS ALLOWABLE ANNUALLY UNDER SECTION 504 (b) OF THE REVENUE ACT OF 1932 FROM GIFTS TO ANY ONE TRUST

Section 504 (b) of the Revenue Act of 1932 excludes from the gift tax the first $5,000 of gifts (other than of future interests) made to any "person" by the donor during the calendar year. Sec-

tion 1111 (a) (1) defines the term "person" as meaning "an individual, a trust or estate, a partnership, or a corporation." Indeed, a trust is customarily regarded as a separate entity comprised of, but distinct from, the trustee and the beneficiaries, and is regularly so treated for tax purposes. And a gift in trust is of course technically made to the trust. Viewing the question from the standpoint of the literal wording of the Act, our position that the trust is the "person" to whom the gift is made, is, therefore, entirely sound.[5] See *Commis-*

[5] The committee reports might be thought to show that the committees regarded the *cestui qui trust* as the donee of a gift in trust. In their exposition of Section 501, which imposed the tax, both the committee reports state (H. Rep. No. 708, 72d Cong., 1st Sess., pp. 27–28; S. Rep. No. 665, 72d Cong., 1st Sess., pp. 39–40):

"The words 'transfer * * * by gift' and 'whether * * * direct or indirect' are designed to cover and comprehend all transactions (subject to certain express conditions and limitations) whereby, and to the extent (sec. 503) that, property or a property right is donatively passed to or conferred upon another, regardless of the means or the device employed in its accomplishment. For example, (1) a transfer of property by a corporation without a consideration, or one less than adequate and fully in money or money's worth, to B would constitute a gift from the stockholders of the corporation to B; (2) a transfer by A to a corporation owned by his children would constitute a gift to the children; (3) a transfer of property to B where there is imposed upon B the obligation of paying a commensurate annuity to C would be a gift to C; (4) the payment of money or the transfer of property to B in consideration whereof he is to render a service to C would constitute a gift to C or gifts both to B and to C depending on whether the service to be rendered by B to C was or was not an adequate and full

sioner v. *Wells*, 88 F. (2d) 339, 340–341 (C. C. A. 7th); *United States* v. *Ryerson*, 114 F. (2d) 150, 154–155 (C. C. A. 7th), certiorari granted, No. 495, this Term, to be argued herewith; *Commissioner* v. *Krebs*, 90 F. (2d) 880 (C. C. A. 3d).[6]

consideration in money or money's worth for that which was received by B; (5) the forgiveness or payment by A of B's indebtedness would constitute a gift to B; (6) where A creates a joint bank account for himself and B, there would be a gift to B when he draws upon the account for his own benefit to the extent of the amount drawn out; (7) where A creates a revocable trust naming B as beneficiary, a gift to B of the corpus is effected when A relinquishes the power to revoke or the power is otherwise terminated in B's favor (the income payments to B in the interim being gifts from A in the calendar years when received)."

It is plain from the quoted language itself, however, that the reports were concerned with the possibility of evasion of the gift tax, and were not considering whether in the case of gifts in trust the trusts or the beneficiaries were the donees for the purpose of determining the number of exclusions under Section 504 (b).

[6] The leading case to the contrary is *Welch* v. *Davidson*, 102 F. (2d) 100 (C. C. A. 1st). As pointed out by Judge Sibley in a concurring opinion in *Hutchings* v. *Commissioner*, 111 F. (2d) 229, 231, the *Davidson* case "rejected the idea that the trust was the donee, and by confusing the trust with the trustee, (who of course takes title only and no beneficial interest), asserted that the beneficiaries are always the donees." The *Davidson* case was thereafter followed in the other cases, *supra*.

Judge Sibley was of the view that the donor's intention should be controlling as to whether the trust or the beneficiary is the donee. He said (111 F. (2d) at 231):

"If it appears that some enterprise or charity or impersonal purpose, or even remote and unascertained first beneficiaries, furnished the motive for the gift in trust, it should be esteemed a single gift to the trust. If on the other hand

The position that the trust should be considered as the "person" or donee for the purpose of determining the number of exclusions is also the more practicable rule administratively, since it avoids the necessity of determining the number and identity of the beneficiaries and the nature or value of their separate interests in each gift. How difficult such determinations frequently are is well illustrated by the present case. The trust instrument creating the 1932 trust provided that for a period of ten years from its date of execution the income should be accumulated, and that at the expiration of the ten-year period the trustee should pay an equal *pro rata* share of the income to each of the grandchildren who were then living and twenty-one years of age, and that as each grandchild reached twenty-one years of age thereafter the trustee should pay his share of the income to him (R. 5). The trust instrument further provided that grandchildren born subsequent to its execution but during the life of the trust (i. e. until twenty-one years after the death of the last survivor of the grandchildren living at the creation of the trust) should be entitled to participate in the trust estate equally with the other grandchildren (R. 5–6).

the first beneficiaries are ascertained individuals whom the donor wished to help, and used the trust only as a devise to convey or preserve the gift or control its ultimate devolution, the gift is to these persons, anl not to the trust, and there are as many gifts as there are first beneficiaries. * * *"

Finally, the trust prescribed the disposition of the income shares of grandchildren dying during the life of the trust and the distribution of the corpus upon its termination (R. 6).

Under such a trust instrument, there is some difficulty, in the first place, in determining the number and identity of the donees, if the beneficiaries and not the trust are to be considered as the donees. Here the taxpayer claimed and the court below allowed an exclusion for each of the eight grandchildren who were living when the trust was created and who were named in the trust instrument. Whether all eight of them were living at the times of all of the gifts, or whether any additional grandchild or grandchildren had been born, does not appear. Presumably, on the taxpayer's theory, only those grandchildren who were living at some particular date or dates are to be considered as donees for determining the number of exclusions. The decisive date might be that of each gift to the trust, although under the trust instrument grandchildren born after a gift has been made are equal beneficiaries of the trust with those born before. Or perhaps the decisive date might be that on which the donor filed his return, or on which the tax liability was finally settled. Whatever the date might be, no showing was made here as to how many grandchildren were alive on any date.

Far more difficult is the task of determining the value of the separate interest of each beneficiary

in each gift. The taxpayer apparently assumes that each gift in trust has the same value to the beneficiaries as if transferred outright, and that this value is to be allocated equally among the eight named grandchildren. Neither assumption is warranted. It is doubtless true from the standpoint of the trust as donee that a gift in trust has the same value as if transferred outright. But that is not true from the standpoint of the beneficiaries, for the reason, among others, that a dollar in hand is worth more than a dollar payable next year. And if the beneficiaries are the donees for determining the number of exclusions, presumably it is the value of the gifts to the beneficiaries which measures the amounts of the exclusions. It is the first $5,000 of gifts made during the year to any person that is excluded from the gift tax by Section 504 (b), and before $5,000 may be excluded for each beneficiary it becomes necessary to establish that each beneficiary has received a gift of that value to him. And if the beneficiaries are considered the donees, it becomes necessary in any event to value each beneficiary's interest under Section 510, which makes the "donee of any gift" secondarily liable "to the extent of the value of such gift." For it is not to be supposed that the donee is made liable beyond the value of the gift to him.[7] Furthermore the eight named grand-

[7] In this connection it should be pointed out that the trust has the resources with which to discharge the tax liability while frequently, as here, the beneficiaries have not.

children were not the only beneficiaries of the gifts in trust. They received no interest in the corpus, which was not to be distributed until twenty-one years after the death of their last survivor, and their rights in the income were subject to defeasance by death and to proportionate diminution by the births of other grandchildren. Thus the gifts in trust were in part for the benefit of unascertainable persons; to that extent the combined interests of the eight named grandchildren fell short of equalling in value the property transferred, even aside from the lessening of the values of their interests by the postponement of their rights to receive income.

Hence there would have to be computed the value to each beneficiary of each gift at the time of the gift, taking into consideration the fact that receipt of the income by the beneficiaries is to be postponed for varying periods. But that is only the beginning of the inquiry. The value of each gift to each beneficiary depends, not only on how much time must elapse before he could receive income, but on how many other beneficiaries would precede him in the receipt of income. The mortality tables would have to be consulted, for the death of any grandchild would terminate his receipt of income, but would, if he died without issue, increase the income of the survivors. The interest of each grandchild would be diminished by the subsequent birth of other grandchildren.

To determine the value of each gift to each living grandchild it would therefore be necessary to compute the probabilities of the births of other grandchildren, including both the number and the dates of births—for the later they were born the less they would subtract from the income rights of grandchildren theretofore born.[8]

This problem of valuation may be approached from another angle, which likewise fortifies the conclusion that if the beneficiaries are the donees exclusions may not be taken on the basis of the face amounts of the gifts. We contend in part II hereof that unless the trust is the donee the gifts

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[8] In *Humes* v. *United States*, 276 U. S. 487, the court held that a deduction for a conditional charitable bequest was properly disallowed because the present value of the bequest could not be determined with approximate accuracy. The taxpayer's valuation involved, as would be necessary here, a combination and adjustment of standard mortality tables and not-so-standard marriage and fertility tables, the latter being based on the experience of Scotch peers. The Court, through Mr. Justice Brandeis, said (pp. 493–494):

"It was on such data that the petitioners sought to set a money value on the probability that this Texas girl of fifteen will not marry, or if she does, will die without issue before the age of thirty, or thirty-five, or forty. Obviously, the calculation that the contingent interest of the charities was equal to 4.0909 per cent of the residue, was mere speculation bearing the delusive appearance of accuracy.

"One may guess, or gamble on, or even insure against, any future event. The Solicitor General tells us that Lloyds of London will insure against having twins. But the fundamental question in the case at bar, is not whether this contingent interest can be insured against or its value guessed at, but what construction shall be given to a statute."

to the 1932 trust were entirely of future interests. But aside from this contention it cannot be questioned that the gifts are in part gifts "of future interests in property" from which no exclusions may be taken. The interests in the corpus, which is to be distributed twenty-one years after the death of the last survivor of the grandchildren living at the creation of the trust, are future interests. So also there are future interests in the income, i. e., the interests of those possible recipients who were unidentifiable at the times of the gifts, such as after-born grandchildren or issue of grandchildren living at the times of the gifts but deceased thereafter. To the extent that the gifts are thus of future interests in property, exclusions may not be taken. *Gardner* v. *Commissioner*, 41 B. T. A. 679, 685.[9] And the value of these interests must on any theory be deducted from the value of the property transferred in determining the amounts of the exclusions.

[9] In that case the trust instrument provided that the income was to be paid to a single named beneficiary for life or for twenty-five years, whichever was shorter, and that after twenty-five years, if the beneficiary was still living, the trust corpus should be given to him. The Board held that the beneficiary's interest in the income was a present interest but that his interest in the corpus was a future interest, that the gifts to the trust were thus in part of a future interest, and that the exclusions were limited in amount to the present value of the beneficiary's right to receive income from the gifts.

In short, we submit that in the case of any trust of average complexity, such as that here, it is impossible to determine the present value to each beneficiary of gifts to the trust. Here the taxpayer has made no effort to show the value of each gift to each beneficiary; and plainly no reasonably accurate showing could be made. Certainly it may not be assumed, as the taxpayer apparently assumes, that each of the eight named grandchildren received in value one-eighth of each gift. Hence the taxpayer has wholly failed to show that each of the eight grandchildren—the named donees—received in the years in question gifts of a value of $5,000.

In addition to these obvious and abundant problems which are avoided by considering the trust as the person to whom the gifts are made, such a construction also eliminates in the case of all gifts in trust the question, discussed in part II hereof, whether the gifts are of present or of future interests. For, as held in the *Wells* and *Krebs* cases, if the trust is the donee, it takes a present interest.

It is true, as has already been stated (*supra* pp. 15–16), that this interpretation of Section 504 (b) makes it possible for a donor to avoid taxes by creating a number of trusts for one person and claiming an exclusion for each trust. However, this gap has now been closed by Section 505 of the Revenue Act of 1938, which amended Section 504 (b) of the 1932 Act to allow no exclusion at all for gifts

in trust. While this amendment applies only to 1939 and subsequent years, it is probable that an overturning of the Bureau's construction at this date would come too late to permit collection now of gift taxes for 1938 and the years before that.

II

THE GRANDCHILDREN RECEIVED FUTURE INTERESTS IN THE PROPERTY CONVEYED TO THE 1932 TRUST

Section 504 (b) excepts gifts "of future interests in property" from the $5,000 exclusion. If, as we contend, the trusts are the persons to whom the gifts are made, there arises no question whether the gifts were of future interests, for the trusts, as entities, took present interests. If, however, as the court below held, the beneficiaries are to be treated as the donees for the purpose of determining the number of exclusions allowable, then it is the character of their interests which determines whether the gift is a gift of a present or of a future interest. We submit that in the instant case the beneficiaries of the 1932 trust received only future interests in the gifts made to that trust, and that therefore no exclusions were allowable. We think it quite probable, although more doubtful, that the beneficiaries of the 1934 trust also took only future interests; that question, however, is academic, since the exclusions allowed below for those beneficiaries are supportable in any event by the direct gifts to them.

As has been pointed out, *supra* pp. 23–26, undoubtedly the gifts to the 1932 trust were in part of future interests; the only question is whether the rights of the eight named grandchildren to receive income from the gifts gave them present or future interests therein. We contend that they were future interests. The property was conveyed to trustees to accumulate the income therefrom for a period of ten years. During this time the beneficiaries were to receive nothing at all from the trust. They had no right to the present enjoyment of the income and unless they survived the ten-year period would never receive any part of the income. We do not believe that it is material whether the eight named grandchildren each had a vested interest in one-eighth of the income from the trust property subject to be totally divested by death or partially divested by the birth of other grandchildren or whether their interests were contingent ones. In either event they were to take effect in enjoyment only in the future and they were, therefore, "future interests" within the meaning of Section 504 (b).

The term "future interests" is, of course, a familiar one in the law of real property, and is frequently defined, expressly or by use, in treatises in that field. These definitions serve, however, only as generally descriptive or to demarcate a field of inquiry. See e. g. Restatement of Property, Vol. II, pp. 516–517. So far as this usage is relevant here,

it probably supports our contention.[10] Here, however, the real question is what Congress meant by the words "future interests in property" in Section 504 (b). Compare *Helvering* v. *Hallock,* 309 U. S. 106, 118. The report of the House Committee states (H. Rep. No. 708, 72d Cong., 1st Sess., p. 29):

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[10] Professors Burdick and Bigelow describe as a future "estate" or "use" a grant, before the statute of uses, of land "to B. for the use of C. to commence ten years hence." Burdick, Real Property (1914) § 150, p. 372; Bigelow, Cases on Property (1919), p. 79.

The Restatement of Property, Vol. II, § 153, in differentiating present and future interests, states:

"(3) A present interest is an interest in land, or in a thing other than land, which includes

"(a) either a right to the immediate beneficial enjoyment of the affected thing;

"(b) or, if the affected thing is the subject matter of a trust,

"(i) either the right to the immediate beneficial enjoyment of the proceeds of the trust;

"(ii) or the right of the trustee forthwith to have the control and management of the affected thing pursuant to the provisions of the trust."

The comment on this provision reads (p. 524):

"*i. Present and future interests when a trust exists.* The rule stated in Subsection (3) (a) is expressed in terms of a 'right to the immediate beneficial enjoyment of the affected thing.' The rule stated in Subsection (3) (b) does not use this phraseology. The reason for this difference is that the relations which exist between a trustee and his beneficiary make it inapt to speak of either the trustee or the beneficiary as having the 'beneficial enjoyment of the affected thing.' Consequently it is necessary, in such a situation, to recognize the co-existence of two different kinds of 'present interests,' namely the possible beneficiary's right to the im-

By subsection (b) a gift or gifts to any one person during the calendar year, if in the amount or of the value of $3,000 or less, is not to be accounted for in determining the total amount of gifts of that or any subsequent calendar year. Likewise, the first $3,000 of a gift to any one person exceeding that amount is not to be accounted for. Such exemption, on the one hand, is to obviate the necessity of keeping an account of and reporting numerous small gifts, and, on the other, to fix the amount sufficiently large to cover in most cases wedding and Christmas gifts and occasional gifts of relatively small amounts. The exemption does not apply with respect to a gift to any donee to whom is given a future interest. The

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mediate beneficial enjoyment of the proceeds of the trust [see Subsection (3) (b) (i)] and the trustee's right forthwith to have the control and management of the affected thing pursuant to the provisions of the trust. * * *"

Thus this analysis is approximately ours, viz, that the trust (or the trustee) received a present interest, so that an exclusion is allowable if it (or he) is viewed as the donee, but that the beneficiaries did not receive present interests because they did not reserve the "right to the immediate beneficial enjoyment of the proceeds of the trust," so that if they are viewed as the donees no exclusions are allowable.

Again, the interest of the beneficiaries here might be compared to "a postponed right to the enjoyment of an easement, profit, rent or similar interest in the land of another." Restatement of Property, Vol. II, § 153 (2). The Restatement recognizes that such interests are analytically "future interests," although for "pragmatic" reasons it excludes them from its definition of the term. See Restatement, Property, Vol. II, pp. 523, 516, 517.

> term "future interests in property" refers to any interest or estate, whether vested or contingent, limited to commence in possession or enjoyment at a future date. The exemption being available only in so far as the donees are ascertainable, the denial of the exemption in the case of gifts of future interests is dictated by the apprehended difficulty, in many instances, of determining the number of eventual donees and the values of their respective gifts.

The Senate Committee increased the exemption to $5,000; otherwise its report repeats the House Committee report quoted above. See S. Rep. No. 665, 72d Cong., 1st Sess., p. 41.

The committees thus described as a future interest any interest "limited to commence in possession or enjoyment at a future date." This definition of future interests is likewise found, in almost identical language, in the Treasury regulations. See Regulations 79, 1933 and 1936 editions, Article 11, set out *infra*, pp. 42, 44–45. These regulations have been in force ever since 1933. In 1938, as has already been seen, Section 504 (b) was amended to eliminate any exclusion from gifts in trust. But the phrase "future interests in property" was retained without amendment. Accordingly, under the familiar rule, the Treasury definition of that phrase was impliedly sanctioned by Congress.

In this case the interests of the beneficiaries of the 1932 trust were not to commence in possession or enjoyment until at least ten years after the creation of the trust. The eight named grandchildren were not to receive their respective shares of the income until that date, or until they were twenty-one, whichever was later. While all the income during the ten-year period, and the undistributed income thereafter, was to be added to the corpus of the trust, and in that way would increase the potential income share of each beneficiary, that income was nonetheless postponed in enjoyment to the beneficiaries. Any beneficiary who died before the date on which he was to receive income would never receive anything. Plainly these beneficiaries received nothing but future interests in the gifts, as that term was used by Congress.

The same result is reached when we look to the end which the committees said they sought to achieve, i. e., avoidance of the difficulty of determining "the number of eventual donees and the values of their respective gifts." How difficult, and as to value probably impossible, that would be in this case and in other similar cases, if the beneficiaries are to be considered the donees, is fully shown, *supra*, pp. 22–27. And it is precisely those problems which Congress sought to obviate. They can be avoided in this case, and in all cases of gifts in trusts, by considering the trust as the donee, as urged in point I of this Argument. But Congress

intended to eliminate these difficulties not alone in the case of gifts to trusts but with respect to direct gifts too, and it sought to do so by excepting gifts of future interests from the $5,000 exclusion.

The court below did not proffer a rationale of its holding that the grandchildren received present interests, but merely quoted and digested various other cases in which it had been held that the beneficiaries of the particular trusts there involved received present interests. See R. 13–16. Of the cases cited, in *Commissioner* v. *Wells,* 88 F. (2d) 339 (C. C. A. 7th), as already stated, the court held that since the trust was to be regarded as the donee the gift was not of a future interest, regardless of the nature of the interests of the beneficiaries. The court also so held in *Commissioner* v. *Krebs,* 90 F. (2d) 880 (C. C. A. 3d), but it went on to say that tested by the nature of the beneficiaries' interests, the gifts there involved were gifts of present interests. In the *Krebs* case, and in the remaining cases cited below (*Noyes* v. *Hassett,* 20 F. Supp. 31 (D. Mass.); *Rheinstrom* v. *Commissioner,* 105 F. (2d) 642 (C. C. A. 8th); *Welch* v. *Davidson,* 22 F. Supp. 726, affirmed on another ground, 102 F. (2d) 100 (C. C. A. 1st)), the trust instruments provided for the distribution of income to the beneficiaries commencing immediately, and for the eventual distribution, after some years, of the corpus. In some of these cases the beneficiaries had an absolute right to income, in others distribution

was left to the discretion of the trustees, but in all whatever right to income the beneficiaries had commenced at once and not at some future date. In this respect these cases are, therefore, distinguishable from the present.

We think, however, that these cases are wrongly decided, and that the correct view is that ably presented by Judge Woodrough in his dissenting opinion in *Rheinstrom* v. *Commissioner,* 105 F. (2d) 642 at 648–650. Judge Woodrough points out, what is well known, that the gift tax was enacted to supplement the estate tax.[11] From this he concludes that the purpose of Congress in excluding the first $5,000 of gifts to any one person other than of future interests in property was to differentiate between "current bounties" and gifts comparable in result to testamentary dispositions.

> Congress looked to the predominant characteristic of those gift transfers that do not work out like testamentary dispositions and which ought not to be taxed like inheritances. It observed that the distinguishing feature is that the donees get such gifts at the time they are made and for present enjoyment.

On the other hand—

> Transfers of property upon trusts that insure to the objects of a man's bounty nothing in the present but an interest in and in-

[11] See H. Rep. No. 708, 72d Cong., 1st Sess., pp. 28–29; S. Rep. No. 665, 72d Cong., 1st Sess., pp. 40–41; 75 Cong. Rec. 5691, 5788, 7239, 10084.

come from his property in the future or after the donor's death, work out results like testamentary provisions and descent laws. Congress wanted and had a right to exact tax on inheritances, and it wanted to and had the same power to exact the tax on transfers that accomplish effects similar to letters testamentary and descent laws. The salient and universal characteristic of the transfers that do accomplish such effects is the preservation of the interest in property to the object of the bounty into the future. Therefore, as to those transfers that do provide for the future interests, Congress plainly said that they should be taxed. The words it used to make an exception to the exemption, "other than future interests in property", seem to me to convey the true intent too plain for argument. The phrase is not of technical significance or used in law like "estates in futuro." It is a layman's expression that every man on the street knows of. Who does not know the difference between getting his property now and getting future interests in it tied up so that he can't get his hands on it till he's old?

The committee reports support this construction of the Act. The committee references to "numerous small gifts" and to "wedding and Christmas gifts and occasional gifts of relatively small amounts" show that they intended to exclude from the tax what Judge Woodrough calls "current bounties." Correlatively, the descriptions of fu-

ture interests as any interests "limited to commence in possession or enjoyment at a future date" and the statements that the denial of the exclusion in the case of gifts of future interests would avoid difficulties of determining "the number of eventual donees and the values of their respective gifts" show that Congress meant to tax in their entirety gifts looking to future earnings and corpus that may exist in the future. The utter fatuity of a contrary result is illustrated by the Board's decision in *Gardner* v. *Commissioner*, 41 B. T. A. 679, 685. There a single beneficiary was to receive the income for 25 years, and then the corpus, if he were still living. The Board held that the beneficiary had a present interest in the income, but a future interest in the corpus, and that the exclusion must be limited to the present value of the right to receive income from the gifts. Plainly it is artificial to hold that the beneficiary had a present interest in the income to be received in the twenty-fourth year, but a future interest in the corpus payable to him the twenty-fifth year. Realistically he had no present interest in either.

Finally, as Judge Woodrough also points out, this interpretation of the Act is necessary if, as Congress intended, the gift tax is "to discourage transfers for the purpose of avoiding the estate tax." (House Committee Report, p. 28, Senate Committee Report, p. 40.) Judge Woodrough said (105 F. (2d) at 650):

* * * But it was obvious to Congress that a living man can multiply his gift transfers to the limit of his estate. Manifestly, if Congress let him make $5,000 transfers of the kind that work out effects like testamentary dispositions without liability for tax, then all he had to do was to multiply and split his transfers and in that way effectively insure the future interests of his heirs presumptive without liability for any tax. Can it really be thought that such was the intent of Congress?

CONCLUSION

For the reasons stated we submit that the decision of the court below is erroneous and that it should be reversed.

Respectfully submitted.

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DECEMBER 1940.

APPENDIX

Revenue Act of 1932, c. 209, 47 Stat. 169:

SEC. 501. IMPOSITION OF TAX.

(a) For the calendar year 1932 and each calendar year thereafter a tax, computed as provided in section 502, shall be imposed upon the transfer during such calendar year by any individual, resident or nonresident, of property by gift.

(b) The tax shall apply whether the transfer is in trust or otherwise, whether the gift is direct or indirect, and whether the property is real or personal, tangible or intangible; but, in the case of a nonresident not a citizen of the United States, shall apply to a transfer only if the property is situated within the United States. The tax shall not apply to a transfer made on or before the date of the enactment of this Act.

* * * * *

SEC. 502. COMPUTATION OF TAX.

The tax for each calendar year shall be an amount equal to the excess of —

(1) a tax, computed in accordance with the Rate Schedule hereinafter set forth, on the aggregate sum of the net gifts for such calendar year and for each of the preceding calendar years, over

(2) a tax, computed in accordance with the Rate Schedule, on the aggregate sum of the net gifts for each of the preceding calendar years.

GIFT TAX RATE SCHEDULE

(There follows a tax rate schedule, the rate being graduated upward according to the amount of the net gifts.)

* * * * *

SEC. 504. NET GIFTS.

(a) *General Definition.*—The term "net gifts" means the total amount of gifts made during the calendar year, less the deductions provided in section 505.

(b) *Gifts Less Than $5,000.*—In the case of gifts (other than of future interests in property) made to any person by the donor during the calendar year, the first $5,000 of such gifts to such person shall not, for the purposes of subsection (a), be included in the total amount of gifts made during such year.

* * * * *

SEC. 510. LIEN FOR TAX.

The tax imposed by this title shall be a lien upon all gifts made during the calendar year, for ten years from the time the gifts are made. If the tax is not paid when due, the donee of any gift shall be personally liable for such tax to the extent of the value of such gift. Any part of the property comprised in the gift sold by the donee to a bona fide purchaser for an adequate and full consideration in money or money's worth shall be divested of the lien herein imposed and the lien, to the extent of the value of such gift, shall attach to all the property of the donee (including after-acquired property) except any part sold to a bona fide purchaser for an adequate and full consideration in money or money's worth. If the Commissioner is satisfied that the tax liability has been fully discharged or provided for, he

may, under regulations prescribed by him with the approval of the Secretary, issue his certificate, releasing any or all of the property from the lien herein imposed:

SEC. 1111. DEFINITIONS.

(a) When used in this Act—

(1) The term "person" means an individual, a trust or estate, a partnership, or a corporation.

* * * * *

Revenue Act of 1938, c. 289, 52 Stat. 447:

SEC. 505. COMPUTATION OF NET GIFTS.

(a) Section 504 (b) of the Revenue Act of 1932, relating to the computation of net gifts, is amended to read as follows:

"(b) *Gifts less than $4,000.*—In the case of gifts (other than gifts in trust or of future interests in property) made to any person by the donor during the calendar year, the first $4,000 of such gifts to such person shall not, for the purposes of subsection (a), be included in the total amount of gifts made during such year."

(b) The amendment made by subsection (a) of this section shall be applied in computing the tax for the calendar year 1939 and each calendar year thereafter (but not the tax for the calendar year 1938 or a previous calendar year), but such amendment shall not be applied in any computations in respect of the calendar year 1938 and previous calendar years for the purpose of computing the tax for the calendar year 1939 or any calendar year thereafter.

Regulations 79, edition approved October 30, 1933. (Promulgated under the Revenue Act of 1932.):

ART. 10. *Total amount of gifts.*—The statute provides that in determining the total

amount of gifts during the calendar year the value of a gift or gifts (other than of a future interest in property) made to any one person is reduced by $5,000. For example, where the donor during a calendar year makes a gift to A of $5,000, a gift to B of $6,000, and two gifts to C of $3,000 each, the total amount of the donor's gifts during such year is $2,000. Gifts made during the calendar year to any one person of $5,000 or less should not be returned unless the gifts consisted of a future interest in property. Gifts of future interests in property are required to be included in the total gifts even though the amount of such gifts is $5,000 or less.

ART. 11. *Future interests in property.*—The gift of a future interest in property, regardless of the amount thereof, is to be included in determining the total amount of gifts made during any calendar year. A future interest in property is any interest or estate in property, whether vested or contingent, which is limited to commence in use, possession, or enjoyment at some future date or time. Gifts of such interests are taxable subject only to the deductions authorized by section 505. For the valuation of future interests, see article 19.

The following example will illustrate the manner of ascertaining the total amount of gifts and the amount of "net gifts" subject to tax: A resident donor gives $10,000 in cash to each of his two sons and conveys, without a valuable consideration, property of the value of $100,000 to a trustee who is to pay the income to the donor's wife during her lifetime and at her death deliver the property to his two daughters. There should be subtracted $5,000 from each of the $10,000 gifts to the sons, and $5,000 from the value of the life estate given to the wife, assuming

that the value of her estate equals or exceeds that amount. The interests of the daughters in the trust property being future interests, no such subtraction is to be made therefrom. The total amount of gifts is $105,000 ($120,000 − $15,000), from which is deductible the specific exemption of $50,000 authorized by section 505 (a) (1). (See article 12.) Assuming the entire $50,000 specific exemption is claimed, the amount of the net or taxable gifts is $55,000.

* * * * *

ART. 20. *Persons required to file return.*—Any individual who was a citizen or resident of the United States and who, within the calendar year 1932 or any calendar year thereafter, makes any transfer or transfers by gift (see article 2) exceeding $5,000 in value to any one person, shall file with the collector a return on Form 709. Any such individual is required to file a return if he makes any gift of a future interest in property regardess of its value. * * *

* * * * *

ART. 21. *Donees and trustees required to file notice of gifts.*—All donees and trustees (except such organizations, etc., referred to in section 505 and article 13) receiving gifts in any one calendar year in excess of $5,000, or gifts of a future interest in property regardless of the value, should file a notice of the receipt of such gifts on Form 710, copies of which may be obtained from the Commissioner, or from any United States collector of internal revenue, upon application. When a gift is made in trust notice thereof should be filed by either the beneficiary of the trust or the trustee, but in such case one notice only is required. * * *

* * * * *

Regulations 79, edition approved February 26, 1936. (Promulgated under the Revenue Act of 1932 as amended and supplemented by the Revenue Acts of 1935 and 1936).

ART. 10. *Total amount of gifts.*—In determining the amount of gifts during any calendar year, there is excluded (save in the case of a gift or gifts of a future interest or interests) the first $5,000 of any single gift or aggregate of gifts made during such year to any one donee. A gift or gifts made during a given calendar year to any one donee of $5,000, or less, should not be listed on the return, unless consisting of a future interest or interests, or unless consisting of a present interest or interests created out of the same property in which a future interest or interests has been given. Gifts of future interests in property are required to be included in the total amount of gifts for the year even though the value of such gifts is $5,000, or less, and if such interest exceeds $5,000 in value, no part of the value is excluded from the total amount of gifts for the year whether the gift or gifts be to a single donee or to a number of donees. For example, if the donor during the calendar year made a gift to A of $5,000 in money, a gift to B of $6,000 in money, and a gift to C of a future interest in property, such future interest being valued at $3,000, the total amount of gifts during such year, for the purposes of the tax, is $4,000.

ART. 11. *Future interests in property.*—No part of the value of a gift of a future interest may be excluded in determining the total amount of gifts made during the calendar year. "Future interests" is a legal term, and includes reversions, remainders, and

other interests or estates, whether vested or contingent, and whether or not supported by a particular interest or estate, which are limited to commence in use, possession, or enjoyment at some future date or time. The term has no reference to such contractual rights as exist in a bond, note (though bearing no interest until maturity), or in a policy of life insurance, the obligations of which are to be discharged by payment in the future. But a future interest or interests in such contractual obligations may be created by the limitations contained in a trust or other instrument of transfer employed in effecting a gift. For the valuation of future interests, see subdivision (7) of article 19.

* * * * *

ART. 20. *Persons required to file return.*—Any individual resident or citizen of the United States who within that portion of the calendar year 1932 subsequent to June 6, 1932, or within any calendar year thereafter, made a transfer by gift to any one donee which exceeded $5,000 in value (or regardless of value if the gift was of a future interest) must file a gift tax return on Form 709. * * *

* * * * *

ART. 21. *Donees and trustees required to file notice of gifts.*—All donees and trustees (except such organizations, etc., referred to in section 505 and article 13) receiving property transferred by gift in any one calendar year, shall file a notice on Form 710, unless the value of the gift, or the aggregate value of all the gifts, to the donee or to any one of the beneficiaries of the trust is $5,000, or less, and the subject of the gift is not a future interest in property. Copies of this form may be obtained from any United States collector of internal revenue upon applica-

tion. When a gift is made in trust notice thereof should be filed by either the beneficiary of the trust or the trustee, but in such case one notice only is required. If property is transferred in trust and the donor retains a power over the property, the notice (which is for information purposes only) should be filed even though it is considered that such power constitutes a retention of beneficial dominion and control and that by reason thereof the transfer is not a gift within the meaning of the statute. * * *

Regulations 79, 1936 edition as amended July 18, 1938. T. D. 4830, Cum. Bull. 1938–2, p. 368: (Amendments to conform the regulations to the Revenue Act of 1938:)

Art. 10. *Total amount of gifts.*—Except with respect to any gift in trust or of a future interest in property, the first $4,000 of gifts made to any one donee during the calendar year 1939 or during any calendar year thereafter shall be excluded in determining the total amount of gifts for such calendar year. Except with respect to any gift of a future interest in property, the first $5,000 of gifts made to any one donee during the calendar year 1938 or during any calendar year prior thereto shall be excluded in determining the total amount of gifts for such calendar year. The entire value of any gift made by a transfer in trust after December 31, 1938, and the entire value of any gift of a future interest in property, must be included in the total amount of gifts for the calendar year in which such a gift is made.

* * * * *

Art. 20. Any individual resident or citizen of the United States who within the calendar year 1939, or within any calendar

year thereafter, makes a transfer or transfers by gift to any one donee of a value or total value of more than $4,000 (or regardless of value in the case of a gift in trust or of a future interest in property), must file a gift tax return for such year on Form 709. In the case of a transfer or transfers by gift to any one donee of a value or total value of more than $5,000 (or regardless of value if the gift was of a future interest in property), made by any individual resident or citizen of the United States during the portion of the calendar year 1932 subsequent to June 6, 1932, or during any calendar year thereafter prior to the calendar year 1939, the filing of a gift tax return on Form 709 by the donor for such year is required.

* * * * *

ART. 21. An information return or notice on Form 710 must be filed by every donee or trustee (except in the case of a gift for a public, charitable, etc., purpose as described in article 13) to whom is transferred in any one calendar year property by gift for which, as set forth in article 20, the donor is required to file a gift tax return.

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IN THE

Supreme Court of the United States

October Term, 1940.

NO. 393.

The United States, *Petitioner,*

v.

Arthur Pelzer.

Petition for a Writ of Certiorari to the Court of Claims.

RESPONSE OF ARTHUR PELZER TO PETITION FOR WRIT OF CERTIORARI.

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RESPONSE OF ARTHUR PELZER TO PETITION FOR WRIT OF CERTIORARI.

The conflict relied upon by the petitioner for the issuance of a writ of certiorari relates only to the holding of the Court below that under Section 504(b) of the Revenue Act of 1932 respondent was entitled to an exclusion of $5,000 for each beneficiary of the trusts in the computation of the net amount of gifts to persons specifically named as being the donees of the gifts.

The position of petitioner is that the trustee named in the trust instrument is the "person" to whom the gifts

were made; and that the trusts are the "donees" of the gift. On that issue there is a conflict with the decision of the Circuit Court of Appeals for the Seventh Circuit in *United States* v. *Ryerson*, decided July 9th, 1940; but on the issue raised by the second specification of error in the petition for certiorari there is no conflict, and it would appear that the writ granted should be limited to the issue raised by the first specification of error. The petitioner does not give any reason for granting the writ to review the issue raised by the second specification of error; and since that issue is fully covered by the findings of fact by the Court below, it appears to be a question that is not open for review by writ of certiorari.

CONCLUSION.

The conflict relied upon is limited to the question of whether the trust is the "donee", or the "person" to whom an economical or beneficial interest in property is transferred by gift, within the meaning of Section 504(b) of the Revenue Act of 1932. Therefore, we submit that the writ granted should be limited to the issue presented by the first specification of error in the petition.

Respectfully,

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BRIEF FOR RESPONDENT.

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INDEX.

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BRIEF FOR RESPONDENT.

OPINION BELOW.

The opinion of the Court of Claims (R. pp. 19-26) is reported in 31 Fed. Supp. 770.

JURISDICTION

The judgment of the Court of Claims was entered June 3, 1940 (R. p. 28). The jurisdiction of this Court is invoked under Section 3(b) of the Act of February 13, 1925, as amended by the Act of May 22, 1939.

STATUTES AND REGULATIONS INVOLVED

The appendix to brief of the United States correctly states the statutes and regulations involved and we shall not repeat them in our brief.

STATEMENT

The brief of the United States contains a fair statement of the facts involved, with the exception that it says the gifts involved "were made to the trusts", which of course is not true; and with such correction we will not burden our brief with a restatement of the facts.

QUESTIONS PRESENTED

The first question presented is:

(a) Whether eight $5,000 exclusions shall be available during each of the calendar years 1932 to 1935, inclusive, in the case of gifts by the donor to his eight living grandchildren, and

(b) Whether four $5,000 exclusions shall be available during each of the calendar years 1934 and 1935 in the case of gifts by the donor to his wife and three daughters.

The second question presented is:

Whether the gifts to the eight living grandchildren is a present or future interest in property.

SUMMARY OF ARGUMENT

The United States takes the position that where a donor makes gifts to two or more individuals of an economical interest in property, and the gifts are consummated by a transfer of property in trust; that the trust created by the donor is the "donee" of the gifts.

In construing the provisions of Section 504(b) of the Revenue Act of 1932, the Courts have generally held that

term "any person" to whom gifts are made during the endar year means the "individual" whom the donor mes as the object of his bounty, and not the trust created the purpose of consummating the gifts to such indilual of an economical interest in property. (See *Welch Davidson,* 102 Fed. (2d) 100; *Rheinstrom v. Commisner,* 105 Fed. (2d) 642; *Robertson* v. *Nee,* 105 Fed. (2d) 7; *McBrier v. Commissioner,* 108 Fed. (2d) 967; *Hutchgs* v. *Commissioner,* 111 Fed. (2d) 229; and *Early* v. *Reid,* 2 Fed. (2d) 118.)

The only exception to the rule of construction established the above cases is the cast of *United States v. Ryerson,* 4 Fed. (2d) 150, which holds that where gifts to two or ore individuals are made by the transfer of property in ist, the trust created by the donor is the "donee" of the ts of an economical interest in property. Such a rule pears to be out of harmony with the purpose of the atute imposing a gift tax. Such a rule is also out of rmony with the statutory law of Alabama, the domicile the donor and donees and the situs of the property inlved in the gifts. (See Sections 6912 and 6913. Code Alabama, 1923 Edition.)

The United States also takes the position that where inme from property transferred in trust as a gift or gifts to be accumulated for the use and benefit of a minor nee or donees for a period of ten years, as provided by ction 6914 of the Code of Alabama (1923 Edition), witht an intervening prior estate between the donor and the nee or donees specifically named, the gift or gifts are of future interest in property.

8

I

ARGUMENT

Number of Exclusions Available

In the case of a transfer of property in trust by an individual with the object of making a gift to each of two or more persons of an economical interest in the property, no gift is completed unless the donor divests himself of full and complete ownership and control of the property transferred and irrevocably names and designates the person or persons to whom the gifts are made (see *Sanford's Estate* v. *Commissioner of Internal Revenue,* 308 U. S. 39, (84 L. Ed 20).

In the above case it is said that,—

> "When the gift tax was enacted Congress was aware that the essence of a transfer is the passage of control over the economical benefits of property rather than any technical changes in its title." (See *Burnet* v. *Guggenheim,* 288 U. S. 280, 77 L. Ed. 748.)

The *Sanford's Estate case, supra,* is authority for the principle that in a case where gifts are made to two or more persons by the transfer of property in trust there must be an irrevocable designation of the "donees" as the persons to whom the gifts are made, and the principle announced in that case was made the basis of the decisions in the following cases involving indirect gifts completed by the transfer of property in trust by the donor, viz: *Rheinstrom* v. *Commissioner,* 105 F. (2d) 642; *Robertson* v. *Nee,* 105 F. (2d) 657; *McBrier* v. *Commissioner,* 108 F. (2d) 967; *Hutchings* v. *Commissioner,* 111 F. (2d) 229; *Early* v. *Reid,* 111 F. (2d) 218; and *Welch* v. *Davidson,* 102 F. (2d) 100.

The United States does not dispute the fact that the gifts involved in this case were completed by an irrevocable designation of donees, and that the donor divested himself of all ownership or control of an economical or beneficial interest in the property transferred in trust.

In the case of *Burnet* v. *Guggenheim,* 288 U. S. 280, 77 L. Ed. 748, it is said that a tax upon gifts is closely related both in structure and in purpose to the tax upon transfers that take effect at death; and in the case of *Sanford's Estate* v. *Commissioner, supra,* it is held that no gift is completed by the transfer of property in trust so long as the "donor" retains the power to change the names of the persons for whose benefit the is created. In the *Guggenheim case, supra,* it is said that the gift tax statute is aimed at transfers of title that have the quality of a gift of an economical interest in property; and when the power to change the name of the beneficiary of the trust is put beyond recall, the gift is completed. (Cf. *Rasquin* v. *Humphreys,* 308 U. S. 54, 84 L. Ed. 77.)

In the case of gifts made by the transfer of property in trust, it is quite evident that the persons for whose benefit the transfer is made are the "donees" of the gifts, where the power to change their designation as such beneficiary is put beyond recall by the donor; and by Section 504(b) of the Revenue Act of 1932 it is provided that in the case of gifts (other than of future interest in property) made to "any person" by the donor during the calendar year the first $5,000 of such gifts shall be excluded from the total amount of the gifts during such year.

The United States appears to concede that if each beneficiary named by the donor is to be regarded as the donee of gifts to each, such individual is intended by the term "any person" when used in Section 504(b) of the Revenue Act of 1932. It appears that the cases of *Sanford's Estate* and *Guggenheim* supra require that a trust must have irrevocable beneficiaries other than the donor, in order to complete a gift by the transfer of property in trust; and where the gift in trust is put beyond the recall of the donor, the beneficiaries named are the donees of the gifts. In the case of *Rasquin* v. *Humphreys,* 308 U. S. 54, 84 L. Ed. 77, it is held that where a trust is irrevocably created, but the donor retains the right to designate new beneficiaries of the trust,

no gift is completed. In the *Humphreys case* the Court says:

> "For the reasons stated in our opinion in the Sanford Case we conclude that the reserved power in the donor at the time of the creation of the trust rendered the gift incomplete and not subject to the gift tax."

Since the irrevocable designation of a beneficiary of the trust is essential to the completion of a gift by the transfer of property in trust, and such beneficiary must be a person other than the donor, it is quite evident that the beneficiary of a trust is the "person" to whom the gift is made. (See *Welch* v. *Davidson, supra.*)

The transfers in trust by the donor to carry out his intent to make gifts of an economical interest in property are controlled by the rules of property applicable to the State of Alabama. Section 6912 of the Code of Alabama (1923 Edition) provides that where real estate, or the income therefrom, is transferred in trust for the use and benefit of a third person, the beneficiary becomes the absolute owner of the property in fee and *no estate or interest vests in the trustee;* and Section 6913 of said Code provides that nothing in Section 6912 shall prevent the conveyance of real or personal property, or the issue, rents and profits thereof, to another *in trust* for the use of the grantor, or his family, or a third person, or for any other lawful purpose; but in such case the *legal title* only shall vest in the trustee.

In order to carry out the intent of Congress when the gift tax was enacted it is not necessary to take into consideration any technical change in title to property. (See *Burnet* v. *Guggenheim*, 288 U. S. 280, 77 L. Ed. 748; *Sanford's Estate* v. *Commissioner*, 308 U. S. 39, 84 L. Ed. 20.)

The provisions of Section 1111 of the Revenue Act of 1932, which provide that "when used in this Act—the term 'person' means an *individual,* a trust or estate, a partnership, or a corporation", should not be given a construction that will defeat the donative intent of the taxpayer in the

case of gifts; and especially so when it is expressly provided that gifts to "any person" of $5,000 or less during any calendar year shall not be subject to tax. The beneficiary of a trust, as the donee of a gift, is an "individual" included in the term "person" when used in the Act; and it appears more sensible to say that the term "any person" when used in Section 504(b) refers to the "individual donee" designated as the beneficiary of the gift rather than the trust which acquires *no economical interest in the property transferred*. (See Section 6913 of the Code of Alabama; 1923 Edition, and *Crook* v. *Harrelson*, 282 U. S. 55, 75 L. Ed. 156.)

We submit that the Court of Claims did not err in allowing one $5,000 exclusion for each beneficiary during each of the years involved.

II

PRESENT AND FUTURE INTEREST IN PROPERTY

The second question presented deals only with the gifts under the "Children's Trust" and is whether or not the gifts to the eight living grandchildren of the donor, who are specifically named, are gifts of a *present interest* in property.

The argument of petitioner that the gifts to the eight living grandchildren of the donor are gifts of a *future interest* in property is based on the fact that the trust instrument provides that for the first ten year period of the life of the trust the income from the property shall be accumulated, invested and reinvested as a *part* of the trust property, and thereafter as each named and living grandchild of the donor attained the age of 21 years "a grandchild's share" of the net income of the trust property should be distributed to him semi-annually, quarterly or monthly during his natural life. (See Section 6914, Alabama Code, 1923 Edition.)

Treasury Regulations 79, Article 11, promulgated under the Revenue Act of 1932, gives the correct definition of a

future interest in property to be "any interest or estate in property, whether vested or contingent, which is limited to commence in use, possession or enjoyment at some future date or time". However, the essential or basic feature of a future interest in property is that it be a vested or contingent *remainder* supported by a prior particular estate of a present interest. (See Sections 6904 and 6905, Code of Alabama, 1923 Edition.) Under the "Children's Trust" the living grandchildren of the donor are the *first persons* who acquire an immediate ceonomical interest in the property after the ownership of the donor ceases by virtue of the gifts. Their economical interest in the property is *vested,* and becomes *presently operative* as a gift to each of them. (See *Doe* v. *Considine,* 73 U. S. 458, 18 L. Ed. 869; *Crawford* v. *Carlisle,* 206 Ala. 379; *Brown* v. *Fletcher,* 235 U. S. 589, 59 L. Ed. 374; and *Blair* v. *Commissioner,* 300 U. S. 5, 81 L. Ed. 465.) The law does not permit the ownership of property to become vacant. (See Section 6912, Code of Alabama, 1923 Edition.)

During the first ten year period of the life of the trust, the net income from the trust property for each of said years is to be invested and reinvested for the *benefit* of the life beneficiaries, and the enjoyment of the economic benefits accruing to them by virtue of the investment and reinvestment of the income in other property in which they have the *present right* to receive the income when they attain the age of 21 years is *realized* by them as completely as it would be if distributed to them in the year earned and expended for the purpose of accumulation as provided in the trust instrument. Even though the life beneficiaries of the trust do not *receive* a distribution of the income while they are minors, they derive money's worth when such income is used to acquire property in which they have an *economical interest.*

Section 6914 of the Code of Alabama (1923 Edition) provides:

> "No trust estate for the purpose of accumulation only can have any force or effect for a longer term than ten years, unless for the *benefit* of a minor in *being* at the date of conveyance, or if by will, at the death of the testator; in which case the trust may extend to the termination of such minority".

The accumulation in the case of the estate of the "Children's Trust" for a period of ten years is for the benefit of the minor beneficiaries *in being* at the date of the conveyance and continues until they attain majority; and the conveyance being irrevocable, it becomes presently operative as a gift to each of them of an economical interest in the property.

Moreover, Section 6915 of the Code of Alabama (1923 Edition) provides:

> "When a minor for whose benefit an accumulation has been directed is destitute of other sufficient means of support and education, the appropriate Court, upon application, may direct a suitable sum to be applied thereto out of the fund."

The State of Alabama has the power to prescribe the conditions of a trust for the benefit of minors, and expressly provides that they shall immediately possess the right to enjoy the use at any time such use may be needed to satisfy the security of support that it affords to them. There is, therefore, no element of futurity in the gifts involved in the "Children's Trust"; and under the law of Alabama there can be none, notwithstanding the able argument of the Solicitor General to the contrary in the brief for the United States.

In the case of *Helvering* v. *Horst*, decided by the Supreme Court on November 25, 1940, it is said that income from property is enjoyed by a person when there accrues to him an economic benefit by virtue of its use; and that it is realized as completely as it would have been if he had collected the income in dollars and expended them for the

purposes named. (See *Old Colony Trust Company* v. *Commissioner,* 279 U. S. 716; *Corliss* v. *Bowers,* 281 U. S. 376; *Burnet* v. *Wells,* 289 U. S. 670.)

Each of the living grandchildren of the donor acquired a *present* right in the trust property to compel the trustee to observe and strictly comply with the terms of the trust and the laws of the State of Alabama in the administration of the trust property, and they were the only persons who *possessed* or *enjoyed* that right in the property. The investment and reinvestment of the income from the trust property for the period of accumulation was not to be enjoyed or realized by the donor; but it is enjoyed by the life beneficiaries of the trust by virtue of their right to have the income from the property acquired by its use paid over to them when they have reached the age of 21 years. In collecting the income from the trust property for the period of accumulation and investing it, the trustee of the property is acting as the agent of the *cestuis que trusts.*

In the case of *Commissioner* v. *Kreb,* 90 Fed. (2d) 881, the Court said:

> "We are further of the opinion that tested by the nature of the gifts to the cestuis que trusts, the donor was entitled to the deduction. The donees were named, the respective values of the gifts to them were ascertainable, and they were given the use of the income and of the unexpended accumulated income without an intervening estate, *even though physical possession was postponed.*"

In the *Horst case, supra,* it is said that the right to control the use of property is synonymous with its actual use and enjoyment. The trust instrument certainly vests in the life beneficiaries the present right to demand of the trustee that the trust property be used for the purposes expressed, and for their benefit, subject only to the exercise of discretion by the trustee in making sound investments of the income for the period of accumulation. There is no likelihood that the trustee will violate any of the provisions

of the trust agreement, but its fidelity is under the control of the life beneficiaries which control they enjoy by virtue of the gifts to them from the earliest moment of time that the gifts were completed and became operative by the transfer of property in trust for their benefit by the donor. The right of the life beneficiaries to demand of the trustee a faithful execution of the trust agreement, and to use the property for their benefit as provided by law is not limited to commence in use or enjoyment at some future date or time.

In the case of a future interest or estate in property, limited to commence in use at some future time or date, there is always a prior estate of present operation; and in this case it is clear that the life beneficiaries named by the donor are vested with a present economical interest in the property. (See *Sanford's Estate case, supra.*)

The receipt of cash is not the only characteristic of the enjoyment of a present economical interest in property. The ownership of such an interest is to be enjoyed by the donees from the first moment of time that it is irrevocably fixed by a completed gift; and the expenditure of the income from the property to procure other property in which the donees will own an economical interest is a present use of the property by the donees or a use which accrues to their economic benefit. (See *Burnet* v. *Wells, supra.*)

In the case of *Crawford* v. *Carlisle,* 206 Ala. 379 (89 So. 565), it is said that *ownership* of property may not become vacant, and that gifts of property to persons named and living when the gifts are completed are gifts of *present operation* to the persons named.

The brief of the United States speculates on the possibility of the donees of a present interest in property living for such a period of time that the present value of their right to income from the property for life shall equal $5,000; and says that the value of the gifts to them is not susceptible of ascertainment. We think that the statute has taken

care of such a contingency when it provides at Section 506 of the 1932 Act, that:

> "If the gift is made in property, the value thereof at the date of the gift *shall be considered the amount of the gift.*"

Each of the donees acquired a one-eighth share in the value of the property transferred in trust; and inasmuch as the property is appraised as to value, the gift to each was a one-eighth part of such value. The *present value* of the gift to each life beneficiary of the estate, computed upon a different basis than the value of the property transferred, has never heretofore been questioned by the United States; and we submit that the value of the gifts to each of the living beneficiaries is conclusively established by the findings of fact by the Court of Claims of the value of the property transferred in trust. (R. pp. 6 et seq.) The findings of the Court of Claims is also conclusive on the question of the *existence* of each of the donees who acquired a *present interest* in the property at the time of the gifts.

The value of such gifts may subsequently be diminished or it may be *lost entirely;* but such a contingency does not affect the amount of the gifts in the computation of the gift tax, nor does such a contingency affect the exclusion of the first $5,000 value of the gifts made by the donor during each of the calendar years involved.

Section 501 et seq of the Gift Tax Title of the Revenue Act of 1932 does not take into consideration the fact that the completed gift of a *present interest* in property to specifically named persons may subsequently be divested by their death, so as to ripen a remainder or *future interest.* Section 504(b) merely provides that the exclusion of the first $5,000 of the gifts made by the donor is applicable only to the donee who acquires a *present interest* in the property by the gift, and not to the donee who acquires a *future interest.* The exclusion of the first $5,000 of the

gift is a gratuity granted the donor, and should not be whittled away by refined argument.

Much of the brief for the United States is devoted to an academic discussion of matters not material to the two simple questions presented by the assignments of error.

CONCLUSION

The petitioner's brief admits there have been acts of "inconsistency" and "immoderation" on the part of *officials* of the Bureau of Internal Revenue in the administration of the Gift Tax Title of the Revenue Law of 1932, and because of such inconsistencies there is reasonable grounds for taxpayers becoming confused in submitting returns of gifts made; but notwithstanding the presence of such confusion the facts as found by the Court of Claims in this case are ample and adequate for a clear-cut decision of the two questions presented. (See *United States* v. *Wells,* 283 U. S. 102, 75 L. Ed. 867.) Any duplication of the allowable exclusions, which may have resulted from the inconsistent acts of officials of the Bureau should not influence a proper construction of the statute involved.

Respectfully,

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6.4

SUPREME COURT OF THE UNITED STATES.

No. 393.—OCTOBER TERM, 1940.

The United States, Petitioner, *vs.* Arthur Pelzer.	On Writ of Certiorari to the Court of Claims.

[March 3, 1941.]

Mr. Justice STONE delivered the opinion of the Court.

Decision in this case turns on the question whether certain gifts of property in trust for the benefit of several beneficiaries are gifts of "future interests" which, in the computation of the gift tax, are, by § 504(b) of the 1932 Revenue Act, 47 Stat. 169, 247, denied the benefit, otherwise allowed, of exclusion from the computation to the extent of the first $5,000 of each gift "made to any person by the donor" during the calendar year.

Sections 501(a) and 502(1) of the 1932 Act impose for each calendar year a tax upon the net amount of transfers "by any individual . . . of property by gift". For the purpose of computing the tax § 504(b) provides "In the case of gifts (other than of future interests in property) made to any person by the donor during the calendar year, the first $5,000 of such gifts . . . shall not . . . be included in the total amount of gifts made during such year".

In 1932 the taxpayer, respondent here, created a trust for the benefit of his eight grandchildren and any other grandchildren who might afterward be born during the term of the trust. The trustee was directed to accumulate the income for a period of ten years and thereafter to pay an "equal grandchild's distributive share" of the income to each of the named grandchildren who were then living and twenty-one years of age and to pay a like share of income to each other named grandchild for life after that child should reach the age of twenty-one years. Provision was made whereby grandchildren born after the creation of the trust and during its life were to receive like participation in the income of the trust except as to distributions of income made prior to the birth of such after-born grandchildren, and except that the after-born grandchildren should be paid their shares of the income dur-

ing their respective minorities after the termination of the ten-year accumulation period. The trust instrument also made gifts over of the share of the income of each grandchild at death, the details of which are not now material. It was further provided that the trust should terminate twenty-one years after death of the last survivor of the named grandchildren, when the corpus of the trust, with accumulated income, was to be distributed in equal shares among the surviving grandchildren and the issue *per stirpes* of all deceased grandchildren.

During the years 1933, 1934, and 1935 the taxpayer added further amounts of property to the 1932 trust. In 1934 he also made gifts directly to his three granddaughters and created a trust to pay the income in equal shares to his wife and three daughters with gifts over of each share of the corpus of the trust upon the death of the life tenant.

Upon claims for refunds of overpaid taxes upon the transfers made in the years 1933, 1934, and 1935, the commissioner recomputed the tax and allowed one $5,000 exclusion only from the net amounts subject to gift tax given or added in each year to each trust. In the present suit, brought in the Court of Claims, respondent sought to recover overpaid taxes for the years in question on the grounds that the gifts to the beneficiaries were gifts of present not future interests and that the taxpayer in the computation of the tax for each year was entitled to one exclusion of $5,000 for each beneficiary. The court sustained both contentions and gave judgment for respondent accordingly. 31 Fed. Supp. 770. We granted certiorari October 21, 1940, to resolve the conflict of the decision below with that of the Seventh Circuit in *Ryerson* v. *United States,* 114 F. (2d) 150.

The Government challenges both grounds of decision below. It argues that only a single $5,000 exclusion is allowable under § 504(b) from the total gifts made to the trust in each calendar year and that if the gifts are deemed to be made to the named beneficiaries of the trust no deduction can be allowed in the case of gifts to the 1932 trust because they were of future interests for which no exclusion is allowed by § 504(b).

We have this day decided the first question, in No. 419, *Helvering* v. *Hutchings,* in which we held that in the case of gifts in trust the beneficiaries are the persons to whom the gifts are made and that for purposes of computation of the tax § 504(b) excludes the first $5,000 in value of the gift to each beneficiary from the taxable

amount of the gifts made in the calendar year. For the reasons stated in our opinion in that case we hold that the first beneficiaries of the trusts in this case are the persons to whom the gifts were made and that the taxpayer is entitled to the benefit of the $5,000 exclusion for each gift to such beneficiary if it is not of a future interest.

But the Government argues here, as it did below, that the gifts to the beneficiaries of the 1932 trust are of future interests within the meaning of the statute and treasury regulations. While the eight named grandchildren are the first beneficiaries of the trust, and the persons to whom the gifts were made, none of them takes any benefit from the trust before the end of the ten-year accumulation period or until he is twenty-one, whichever last occurs, and then only if he survives that event. And the question is whether such a gift is a gift of a "future interest" within the meaning of §504(b). Respondent, relying on statutes and judicial decisions of Alabama, where the trust was created and is being administered, insists that the gifts to the named grandchildren are present not future interests as defined by Alabama law. He argues that as § 504(b) does not define the "future interests" gifts of which are excluded from its benefits, they must be taken to be future interests as defined by the local law, and it is the local law definition of future interests which must be adopted in applying the section. But as we have often had occasion to point out, the revenue laws are to be construed in the light of their general purpose to establish a nationwide scheme of taxation uniform in its application. Hence their provisions are not to be taken as subject to state control or limitation unless the language or necessary implication of the section involved makes its application dependent on state law. *Burnet* v. *Harmel*, 287 U. S. 103, 110; *Morgan* v. *Commissioner*, 309 U. S. 78, 81.

We find no such implication in the exclusion of gifts of "future interests" from the benefits given by § 504(b). In the absence of any statutory definition of the phrase we look to the purpose of the statute to ascertain what is intended. It plainly is not concerned with the varying local definitions of property interests or with the local refinements of conveyancing, and there is no reason for supposing that the extent of the granted tax exemption was intended to be given a corresponding variation. Its purpose was rather the protection of the revenue and the appropriate administration of the tax immunity provided by the statute. It is this purpose which

marks the boundaries of the statutory command. The committee reports recommending the legislation declared (H. Rept. No. 708, 72d Cong., 1st Sess., p. 29; S. Rept. No. 665, 72d Cong., 1st Sess., p. 41):

"The term 'future interests in property' refers to any interest or estate, whether vested or contingent, limited to commence in possession or enjoyment at a future date. The exemption being available only in so far as the donees are ascertainable, the denial of the exemption in the case of gifts of future interests is dictated by the apprehended difficulty, in many instances, of determining the number of eventual donees and the values of their respective gifts."

Article XI of Treasury Regulation 79, 1933 and 1936 editions, interpreting § 504(b), declared that "future interests" include any interest or estate "whether vested or contingent, limited to commence in use, possession or enjoyment at some future date or time". This definition stands unchanged in the regulations and while § 504(b) was amended by § 505 of the 1938 Revenue Act so as to withdraw the benefit of the $5,000 exclusion from all gifts in trust the section as amended continues to withhold the benefit of the exclusion from all gifts of "future interests in property".

We think that the regulations, so far as they are applicable to the present gifts, are within the competence of the Treasury in interpreting § 504(b) and effect its purpose as declared by the reports of the Congressional committees, and that the gifts to the eight beneficiaries of the 1932 trust were gifts of future interests which are excluded from the benefits of that section. Here the beneficiaries had no right to the present enjoyment of the corpus or of the income and unless they survive the ten-year period they will never receive any part of either. The "use, possession or enjoyment" of each donee is thus postponed to the happening of a future uncertain event. The gift thus involved the difficulties of determining the "number of eventual donees and the value of their respective gifts" which it was the purpose of the statute to avoid.

We have no occasion to consider the definition of future interests in other aspects than those presented by the present case. The judgment of the Court of ~~Appeals~~ Claims will be reversed so far only as it excluded the gifts to the 1932 trust from the computation of the tax for each of the years in question.

Reversed.